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Touche, Ross, Bailey & Smart

TOUCHE, ROSS, BAILEY & SMART

The Quarterly

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The Quarterly

TOUCHE, ROSS, BAILEY & SMART (U.S.A.)
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Firm policies and procedures on technical matters are stated in our technical manuals, bulletins and letters. The opinions expressed herein on technical subjects represent those of the authors and are not to be construed as setting forth new or amending present firm policies and procedures.

Integrated Services

in

by Donald J. Bevis

At the recent Management Conference at The Homestead, there was a good deal of discussion of the "integrated services concept." From the questions raised by the participants in the conference and in other meetings, it is clear that there is still a need for some clarification of this concept, what it is and how it works. That is the aim of this article.

Before going further, I suggest that you reread two articles in the last issue (June, 1963) of THE QUARTERLY—"Organizing the Firm for Growth" by Robert Beyer and "Business Approach to Auditing" by Walter H. Soderdahl. With this as background, we can then deal with some of the questions raised most frequently by TRB&S personnel and clients.

What is Integrated Services?

Integrated services is the term we have adopted to describe our coordinated team approach to the financial management problems of our clients, utilizing our knowledge and experience in the specialized areas of accounting and auditing, taxes and management services. As you will see, the key phrase in this definition of integrated services is "coordinated team approach."

Many problem areas can be individually dealt with by a reasonably curious, informed and skilled auditor. For problem areas requiring special or highly-technical skills, however, the auditor must draw from the array of highly-trained technicians employed by the firm for just this purpose. Experienced financial planners, tax specialists, mathematicians, EDP specialists, etc., skilled in such areas as mergers and acquisitions, tax planning, the application of mathematical techniques to business problems, electronic data processing, and work measurement studies, are available to give maximum assistance to operating management under the concept of integrated services. These talents are available on a coordinated basis.

What is the Need for Integrated Services?

For many years our practice has generally consisted of auditing, tax, and management services in one combination or another. Each of the three has its own special connotation when considered separately. As auditors, we have developed a knowledge of control functions and control techniques. We have also achieved a knowledge of systems designed for financial information. Within the management services field, we have acquired and are continuing to develop the new capabilities required by the demands of modern business. Today, our capabilities include not only financial but other types of information systems. Within the tax field, our talents go far beyond the routine preparation of tax returns; they encompass comprehensive tax planning on both an international and a domestic basis.

With the growth and development of each of these

Action

services, the tendency to specialize has brought about an uncomfortable feeling of compartmentalization. Certainly, the specialization necessary to attain technical competence is required of all members of the firm. But new requirements in one business field after another make it imperative that we take a look at the whole accounting function in terms of the changing environment. When we do this, we see that the accounting function has taken on a broad new countenance to meet the new requirements for measurement and communication of financial and economic data.

Modern business management requires a decision-making process that marshalls all relevant data and develops alternate strategies with predictable consequences. Its ideal is to make decisions based on facts as they exist at the moment of decision. Such a process requires a co-ordinated approach, one best provided by someone who understands *all* the integrated services necessary to arrive at an optimum conclusion. Thus, an integrated accounting service, co-ordinating auditing, tax and management services for every client—all conducted under the same standards of competence, independence and responsibility—is an absolute necessity.

How Will Integrated Services Work?

The key to our concept of integrated services is the "general services partner." As Robert Beyer has stated:

Donald J. Bevis, a fluent speaker on accounting and related subjects, was selected this year for special national recognition by Beta Gamma Sigma on their 50th anniversary. Now senior partner in our Executive office, Mr. Bevis started his accounting career in 1934.

Mr. Bevis is a former vice-president of the AICPA, and the American Accounting Association, and is a past president of the Michigan Association of CPAs. He has served on numerous committees for the Institute and is currently a member of the Committee on International Relations and the Committee on Uniformity of Legislative and Other Standards Governing Practice.

A graduate of the University of Michigan, Mr. Bevis received the Degree of Bachelor of Arts from their College of Literature, Science and the Arts in 1933 and in 1934 received the degree of Master of Business Administration "with distinction" from the School of Business Administration.

"A general service partner is a 'line' executive reporting to the partner in charge of an office. His experience background is such that he is able to deal in some depth with all three classes of service—audit, tax and management services—and he also assumes responsibility for the 'added ingredient' of integration. He has primary and over-all responsibility for the firm's relationship with the client."

Imagine if you will a medium to large sized company, mass-producing and distributing several lines of consumer goods, publicly held, considering moving into other countries, maintaining cost, production and sales data on EDP equipment. It's not too difficult to imagine the many problems such a client might have, even with the best management group.

Being a publicly held company, an annual audit by a firm familiar with SEC requirements would, of course, be necessary. One of the first things that would concern the auditor in his review of accounting procedures and internal control would be the EDP system. Hopefully, he would have the training necssary to perform this review, but he should also be alert to situations requiring study by an EDP expert. He might find that management was not getting valid or useful product cost information from the existing system. Investigation by a specialist in management services could disclose deeper problems in production scheduling, product mix, pricing and other areas subject to management decisions.

The auditor would also be concerned with the accounting and financial reporting implications of the company's projected operations in other countries. In addition to deciding the countries in which to operate, management would have to weigh the advantages of building its own plants or entering into licensing arrangements with foreign manufacturers. Further, should one or more subsidiary corporations be used or would a branch set-up be better? If subsidiaries are to be formed, in what jurisdictions? Obviously, these problems have accounting and auditing implications, as well as tax and management services implications.

I don't think I need go any further with this imaginary company. The point is that businesses today are facing situations of this kind. Small businesses are becoming medium-sized businesses, medium-sized businesses are becoming large businesses, domestic companies are becoming international companies, and at every step along the way management is faced with numerous and varied problems. They are looking for help with these problems.

It is in this environment that the general service partner for each client functions. He has an understanding of the client's business and is in constant touch. He will discuss problem areas with the client and point out where he feels impovements are needed, and how we can be of service. When it appears desirable, the general service partner will call in audit, tax or management services specialists. Working as a team under the direction of the general service partner, these people, together with representatives from the client, will develop and implement appropriate corrective measures or programs for improvement.

Naturally, in our effort to provide integrated services, the general service partner is not the only person with responsibility. On every audit, each person on the job shares this responsibility. While an audit is obstensibly an examination of a client's financial statements, the auditor actually examines the client's business. In the course of making judgments about individual accounts and financial statements as a whole, the auditor comes in close contact with the myriad details of day-to-day operations. He sees materials procured, converted, stored and sold; he sees money received and disbursed; he sees mountains of paperwork processed; he sees people performing all sorts of assignments. This comprehensive and intensive exposure to practically every procedure within a client's business places a curious, informed and skilled accountant in a rare position to observe and evaluate procedures, to identify deficiencies, and to offer constructive suggestions to management to improve operations. These suggestions, often looked upon as an audit "bonus" by the client, are really essential to a good audit. They are what distinguish a "beneficial" audit from that which is purely routine. Unquestionably this comprehensive assistance to management is one of the best ways to build client goodwill.

When reviewing operating procedures and accounting controls, the auditor should continuously ask himself how the client can do a better job, reduce costs, eliminate trouble-spots, or solve special problems. This inquisitive attitude directs the attention of the auditor toward opportunities to be of special service to the client. Not every lead will prove fruitful upon further exploration, but sometimes even apparently barren leads will develop into major service opportunities. Findings and proposed recommendations should be brought to the attention of the general service partners, and if desirable, will be discussed with management services or tax specialists to get the benefits of their experience and viewpoints. In many cases, technical problems will then be discussed with the client by specialists who can proceed with the work required by the client.

Is Integrated Services New?

The idea of utilizing all the firm's specialized services in dealing with the problems of a single client certainly is not new. Nor is the general service partner concept entirely new. Many of our partners have been serving their clients in this capacity for many years.

Nevertheless, there is something new. There is a new emphasis on the importance of carrying the integrated services concept to all of our clients, whether large or small, and there is a new determination to have the type of organization and the kind of people we need to do this.

Where Does the Specialist Fit?

Obviously, we need people with fairly comprehensive knowledge and competence in all of the three principal fields of our practice, as well as in the broad area we commonly refer to as the business world. If such people can also be expert in one or more of the major areas of our practice, they will be all the more valuable. It should be clear that we will always need specialists, for without specialists in accounting and auditing, tax planning, and the various management services, the general service partner would be like a doctor without his medical bag.

As the complexities of modern business demand a higher ratio of expert services, the specialist will become more and more indispensable. As he makes a name in his field, he will receive a reward that is commensurate with his talents. Nor will he be confined to his specialty, for a specialist may well become a general service partner, even though he continues in the specialty of his choice.

How Will Integrated Services Affect You?

We have always expected and encouraged everyone to continue his education long after his formal schooling has ended. This personal effort on the part of each of us will be increasingly important as we emphasize the concept of integrated services. Many, perhaps most, of our staff people will be encouraged to specialize in one of the three principal fields of our practice. There will be an added obligation, however. Every person on the professional staff will be required to learn as much as possible about at least one, and hopefully both of the other fields of specialization.

To help in spotting and developing people with potential for becoming general service partners, we have already instituted new requirements for promotion within the firm. These new requirements were announced in the September, 1962 issue of THE QUARTERLY. I think it would be worthwhile to quote here a portion of that announcement:

"Broad experience for our professional people has always been one of the goals of our firm. With few exceptions it has never been our practice to have people specialize during the earlier years of their career, although we have an urgent need for trained people in each service area. The exceptions have usually involved people with specialized education or experience. During recent years, however, we have become even more aware of the need for the "account executive" or "general services" type of partner and manager. We need people who can be a liaison between the client and every type of service we have to offer: people who can assess any financial problem that comes up in the operation of a business and recommend the specialist or combination of specialists from our firm who are best equipped to deal with it.

"This breadth of experience is no longer an ideal but a necessity if we are to provide our clients with the best possible quality of service. Accordingly, we have formalized our policy of experience requirements for promotion as outlined below.

"All inexperienced staff people employed since January 1, 1962 must meet the broad minimum requirement of having experience in at least two of the three classes of service—audit, tax, and management services —before they are eligible for promotion to Supervisor or Senior Consultant."

Each one of us in the profession of Certified Public Accountants must continue to study and learn if we are to be equal to the challenges and opportunities created by the postwar revolution in information technology. This is of the utmost importance to our clients and hence to the firm and to each of us. By the time a person reaches the level of maturity from which new partners are selected, he should have a comprehensive working knowledge of all of the services we offer. He may be an expert in only one field of our practice, but he will know enough about the other fields to recognize situations where those services will be beneficial to the client.

Business today is calling on us for co-ordination of specialties and it is our responsibility to comply. This we are doing by means of the integrated services concept through the agency of our general service partner. If we do this well, we will attain our growth objectives, we will be better able to reward outstanding individual effort, and most important of all, we will improve our ability to fulfill our obligations to our clients.

Our New Partners . . .

Nine new partners met in New York on August 14th and 15th to sign the Partnership Agreement, meet with the Policy Group and learn about the future plans of the firm. Pictured here, (left to right) are Robert M. Shehan, Chicago; Richard E. Sprague, Executive office, (admitted as Principle); Herbert J. Brewer, Houston; A. Clayton Ostlund, Minneapolis; Glen A. Olson, San Diego; Robert Beyer, Managing Partner; John W. McEachren, Chairman of the Policy Group; Robert Trueblood, Vice-Chairman of the Policy Group; J. Shannon Gustafson, New York
John S. Heil, Jr. Los Angeles; J. Richard Beck, Minneapolis; Loren G. Hoffman, Kansas City.

Robert M. Benjamin * xer file

Auditing automatic source recording

A case study

An employee identification badge and prepunched labor card being inserted into IBM 357 "transactor" source recording device for labor accounting.

Electronic data processing concepts have advanced so much that, if put into practice, they might make conventional auditing of automatic source recording physically impossible. Several writers on the subject have predicted that the conventional auditing techniques can be adapted to the EDP systems in current use as well as those of the future. These adaptations lean heavily on maintaining audit trails and getting readable input and output data.

But a recent case study of an automatic time clock system in a large industrial plant shows the need for a use of a fresh auditing approach. It solves the problem by emphasizing testing of procedures and controls rather than transactions. It appears to be a valid method for application to the "complete" business systems expected to be common in the future.

Before highlighting the case study, we will define the "complete" business systems as being on-the-line-real-time, translating business transactions when they physically take place. They have no audit trails. Input documents are unconventional, almost eliminated. Output information emerges in summary, not detail.

Steps toward the on-the-line-real-time systems taken now by many businesses involve use of either computer systems or semi-mechanized systems such as automatic source recording devices. Examples of such devices are time clocks, the subject of our study, point-of-sale recorders for retailers, the airlines' automatic reservations and ticketing networks.

In our case, the situation confronting the auditors was an automatic time clock system which records labor transactions in a major plant of a large manufacturer. Automatic time recording devices (IBM 357 "Transactors") are located throughout the shop areas. For the 11,600 employees covered by this system, these devices have completely replaced the human timekeepers and manually-prepared time cards.

Data from the system flows through to the company's payroll and job order cost accounting and control records. Basic timekeeping tools are: (1) the plastic employee badge, prepunched with identifying information, and (2) the job card, prepunched with the charge number and other information about a particular job.

The badges are permanently assigned to each employee. The job cards follow the parts or assemblies to be worked on. Exceptions are indirect labor and other special cards, which are located in racks adjacent to the Transactors. Clock-in on reporting for work requires only insertion of the badge into the Transactor, and depression of certain keys. Check-in on a job requires insertion of the badge and one or more job cards, and depression of other keys.

All Transactors are linked electronically to a central control box (IBM 358), a master clock, and an in-line key punch which creates a punched card for each entry. The cards are converted to magnetic tape for passing through computer processes on IBM 1400 Series equipment. The first of these, a match against an employee identification master tape, begins one-half hour after the beginning of each shift.

Within an hour after shift start, an exception report has been prepared for distribution to shop foremen. This report indicates absences, tardy clock-in, preshift overtime, and failure to check in on a job. Each exception must be approved by the shop foreman. Transactions accepted in this first processing routine plus transactions accepted for the remainder of the shift are "posted" to a 1410 random access file arranged by employee. Transactions rejected must be analyzed and corrected for re-entry into the processing cycle.

All labor transactions for the day are read out onto another magnetic tape which goes through a series of further computer processes:

(1) Preparation of final daily report to shop foremen. Again prepared for exceptions only, this shows overtime, early clock-out, and other items for approval by foremen.

(2) Daily report which balances job time by employee with time between clock-in and clock-out.

(3) Daily labor tape prepared after (2).

(4) Matching of job transactions against a random access file of job numbers. This processing involves application of labor standards on certain jobs, accumulation of time by classification, and preparation of output tapes for numerous reports. These include daily reports of actual and budgeted time to certain shops, summary management reports by type of labor, and job status reports.

(5) Entry of the daily labor tape from (3) above into another computer (IBM 7080) for the payroll process. At this point the labor hour transactions are "priced" by application of pay rates. The labor is accumulated by employee for bi-weekly payroll processing and by job for weekly accounting distribution reports.

In pre-EDP days, an auditor was able to begin with either a payroll report or a labor distribution report and to trace individual time charges back through the system to underlying time cards or other source documents. This is obviously impossible when the labor transaction is initiated mechanically.

The auditors decided that their review of labor charges would consist of two phases:

Currently audit manager in the Seattle office, Robert M. Benjamin has responsibility also for the Seattle office staff training, staff scheduling, and report review. He graduated from Washington State University in 1951 with a B.A. degree in English and studied accounting at the University of Washington. He has been with TRB&S since 1953.

He is a former vice president and treasurer of the Seattle Junior Chamber of Commerce, and is a member of the AICPA, the Washington Society of CPAs, the Institute of Internal Auditors, and Beta Alpha Psi.

1. Observance of actual labor charges being initiated, with subsequent tracing of these transactions through to final reports.

2. Test of the system itself in normal operations, by use of dummy but realistic transactions designed to test not only the routine processing but also the various exception editing and rejection procedures.

It was also decided that the second of these phases should receive greater emphasis because it enables many facets of the operation to be tested with only a small number of transactions. An alternate approach would be for the auditor to make a detailed examination of the computer program instructions. However, this would involve a massive translation and interpretation of many thousands of coded individual program instructions.

Consequently, the auditors decided upon the dummy transaction method as equally acceptable but easier than the alternate approach. Steps they followed in using the dummy transaction method included:

1. A thorough review of system and computer program flow charts was made.

2. Inquiry was made of responsible persons as to the various control points designed into the system.

3. Based on the system review, a set of situations was prearranged. These situations were designed to test many of the control points said to exist in the system. Several examples of these situations were:

(a) Employee clocks in on time, works normally for full shift.

(b) Employee checks in on job without clocking in.

(c) Employee clocks in but fails to record a job transaction.

(d) Employee is absent.

(e) Employee is tardy.

(f) Employee is tardy but within three-minute "grace period" allowed.

(g) Employee leaves before shift ends.

(h) Employee leaves early but returns.

(i) Night shift employee clocks in on day shift.

(j) Employee works overtime into next shift.

(k) Employee is loaned to a different shop.

(l) Employee charges jobs improperly (e.g. direct as indirect time).

PROGRAM 0362L — MACCS LABOR BALANCE REGISTER — 702-070

BUDGET LOAN	SHIFT	EIN PROCESS	S.S.N. STAT	FWC	EMPLOYEE NAME CC W.O. SUB SERIAL	OPN RES	CT CC	TIME	HOURS REG	BUN	DATE MO-DY-YR	L/D CARD COUNT	JOB COUNT
2-9251	1	159970	202-28-0826		MCLEAN GARY			09.47	7.0		10-31-62		
2-9251	1	037247Y	55	1331	1-67232-1027-233787	7		11.45	2.0				
2-1860	1	1309174	55	0000	8-25334-1860-000000	000		17.02	5.0			2	2
2-9251	2	159978	541-30-2792		MCLEAN GARY			17.88			10-31-62		
2-9251	2	159979	536-28-6570		MCLEAN GARY						10-31-62	ABSENT	
2-9251	1	159972	535-24-7310		MCLEAN GARY			08.5	8.0		10-31-62		
2-9251	1	1309013	55	0000	1-72823-0940-029251	000		10.93	2.4				
2-9251	1	044859W	55	1341	1-69591-1220-220050	3		13.65	.7				
2-9251	1	012614Z	55	1341	2-78800-0406-507568	675		13.85	.5				
2-9251	1	003865L	55	1341	1-72141-0322-072000	000		13.65	.2				
2-9251	1	003865L	55	1341	1-72141-0322-071000	000		13.65	.3				
2-9251	1	003865L	55	1341	1-72141-0322-072000	000		13.85	.2				
2-9251	1	003865L	55	1341	1-72141-0322-071000	000		13.85	.3				
2-9251	1	103436W	55	1341	1-78900-0201-379106	152		13.65	.3				
2-9251	1	136933U	55	4652	1-78103-0580-064007	014		17.02	2.9				
2-9251	1	136933U	55	4652									
2-9251	1	159971	518-30-7674										
2-9251	1	092586X	55	1323									
2-9251	1	092586X	55	1323									
2-9251	1	1309013	55	0000									
2-9251	1	1309013	55	0000									
2-9251	2	159977	513-20-9504										
2-9251	2	0999566											

GATE REPORT

FIRST SHIFT SUMMARY

G GRACE PERIOD G
T TARDY
R RETURN
EARLY LEAVE E
N - NO - N
Y YES

A - Absent
AP - Away but Paid
E - Early Leave
F - Failure to Punch
H - Hospital, Industrial Accident
JD - Jury Duty
LOA - Leave of Absence
NH - New Hire
SC - Shift Change
T - Tardy
TB - Temporary Badge Used
TI - Transferred In
TO - Transferred Out
V - Vacation

OCT 31, 1962

DATE

AUTHORIZED SIGNATURE

SHIFT	BUDGET ORG'N	STA.	EIN	EMPLOYEE NAME	SOCIAL SECURITY NO.	CLOCK	NORMAL SHIFT START	ACTUAL TIME START	ACTUAL TIME STOP	HOURS PAID REG.	HOURS PAID O.T.	CLOCK IN	JOB CHECK IN	PRESHIFT O.T.	POST-SHIFT O.T. O.T. HOURS AUTHORIZED BY KEYBOARD	POST-SHIFT O.T. N-NO Y-YES	O.T. LUNCH	CLOCK OUT	REMARKS
1	2-9251	55	599706	MCLEAN GARY	202 26	0626	085	0947	1702	7.0		T							LOAN TO 2-9251
1	2-9251	55	599714	MCLEAN GARY	518 30	7674	085	0827	178	8.0	00.8				0.8	9			LOAN TO 2-9251
1	2-9251	55	599720	MCLEAN GARY	535 24	7310	085	085	1702	8.0		N							

The auditor's name and dummy numbers appeared on reports produced by the daily data processing cycle. Above is segment of daily labor balance report. Below is final daily gate report indicating exception transactions to shop foremen.

(m) Employee uses transactor keys improperly when checking in on job.

4. The necessary timekeeping documents were then arranged for and pre-set into the system. Since the auditors desired to perform the test under normal operating conditions, using actual shop locations and job cards, the only dummy items necessary were a group of employee badges. With one exception used for test purposes, the employee information was entered into the master records to agree with the badges. (Similar entry was not made into the payroll master records in order that no paychecks would result. However, it would be possible to carry such a test through the payroll portion of the system.)

5. Using the situations outlined above, and a prearranged time schedule, the test was carried out in two shops during normal working hours. Both day and night shifts were used.

6. Data processing supervisors were made aware of the general nature of the test but not of the specific types of transactions being tested. Shop foremen were not informed until after they had questioned the dummy transactions which appeared as exceptions on attendance reports.

7. All transactions (42 in number) were traced through to reports which emerged from the data processing system on the same and following day. These included preliminary and final attendance exception reports, exception reports of erroneous job transactions, and the daily balance report of proper job and attendance transactions.

8. During the test, observation was made of several employees initiating job transactions. These were likewise traced to daily reports.

9. The auditors utilized the inquiry features of the data processing system to read out sections of the records and determine that the test items were being handled under normal conditions.

The results of the test proved highly satisfactory. The auditors identified, with two exceptions, every dummy transaction as being processed properly, and concluded that the system was generally functioning as it had been outlined. Two system discrepancies were noted.

Extended tests on a subsequent day were made in an effort to determine the reasons for these two discrepancies. The extended tests confirmed the errors and brought about an investigation which disclosed the reasons.

The first discrepancy resulted in the rejection of certain seemingly proper transactions as exceptions. This happened because the manufacturer had previously made a change in "leave early" cards but had failed to collect all the superseded cards from the rack placed in the shop.

The second discrepancy was rather unusual and brought to light a computer programming error. The program instructions said, in effect, "If the next to last employee in the processing cycle is an exception, do not process the last employee." Since the dummy employee numbers used by the auditors were the last on the employee list, this program instruction went into effect and the last item failed to process.

Although the procedures were not designed to test the payroll portion of the system, the auditors did note that all time accumulated for the dummy employees was rejected when the data reached the payroll cycle. This provided assurance that paychecks could be processed only for employees having payroll master records as well as master records in the timekeeping system. Because the files and EDP equipment are physically and organizationally separated, payroll padding would require a considerable amount of collusion.

It should be mentioned here that the audit program for this manufacturer also includes tests which begin at the other end of the payroll cycle—the accounting records. The procedures include reconciling payrolls paid with distributed labor, tracing labor distribution from accounting entries to weekly and daily reports, and the normal testing of employees' payroll records and paychecks. It is felt that the system test of labor collection outlined above provides the auditors with a complete check on the labor system from the point of origin through to the general ledger.

Members of the manufacturer's management responsible for this phase of operations were extremely cooperative in assisting the auditors, and, in fact, welcomed the independent test of computer programs. While the programs were tested thoroughly during their design and implementation phases, this was the first test of the system in actual operation. The responsible persons were particularly interested in the system discrepancies disclosed, and took immediate corrective action.

This auditing project was in many ways experimental. Its success and in particular its comparative ease of performance were gratifying indeed. The number of unusual conditions which were tested with a few simple prearranged plans would have required thousands upon thousands of transaction selections had random sampling or any other conventional testing process been used.

The power of a fresh approach to the problem combined with the effective use of the computer in focusing on controls and exceptions is tremendous. By using his ingenuity and making the computer his tool, the auditor can meet the challenge of the future: maintaining his historically high standard of professional competence.

DOGS ARE NOT HORSES

Mr. Chartac

Fortune recently revealed that 700 of the 6,000 special agents of the Federal Bureau of Investigation are trained as accountants. Detective fiction ought not to lag behind reality. So, as a guide to what may now be expected, here is the first of a series.

I AM NOT of the school of thought that holds that the General Commissioners are not human, but I have always held that due caution and professional dignity make it advisable to behave as if they were not. Then when the lapses into common humanity come they are all the more welcome. It is even possible that a little joke will help. I don't recommend it, but it is possible.

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We are indebted to Accountancy, *the Journal of the Institute of Chartered Accountants in England and Wales, for this reprint from their July '63 issue.*

Examining a Company in Bankruptcy

by Edward A. Weinstein

"The Congress shall have the Power to . . . establish . . . uniform Laws on the subject of Bankruptcies throughout the United States." — The Constitution of the United States, Article I, Section 8.

During the past two years a number of bankruptcies have received considerable publicity. Among the larger recent bankruptcies were:

Grayson Robinson Stores, Inc.
American Dixie Shops, Inc.
Masters, Inc.
Davega Stores, Inc.
Dilbert Bros., Inc.
Dejay Stores, Inc.
Rek-o-Kut Company, Inc.

In almost all bankruptcy cases (usually excepting those involving small companies with negligible estates), independent accountants are appointed by the courts to examine the affairs of the bankrupt companies. The examination of a company subject to the provisions of the Bankruptcy Act varies in scope from the normal audit of a client company. These variances and other factors encountered in this type of examination necessitate a report which is different from the usual audit report.

It is the purpose of this paper to discuss these differences in scope and reporting.

The discussion will be confined to corporate bankruptcies, under the national Bankruptcy Act. References to the Bankruptcy Law are of a general nature to provide the accountant with background information necessary for an understanding of the problems involved in a bankruptcy examination.

The United States Constitution gives Congress the power to establish uniform, nationwide bankruptcy laws. Congress has enacted several bankruptcy laws including the Act of 1898, now in force, amended by the the Act of 1938. The essence of the Bankruptcy Act of 1898 is incorporated into Chapters I through VII of the Act of 1938.

The bankruptcy laws are designed to afford the debtor some relief from his creditors, the relief varying from complete discharge from all debts to a reduction and/or rearrangement of some debts. Bankruptcy, in its various forms, is a privileged status under which the debtor attempts to reorganize or liquidate his affairs while under the protection of the court. A feature common to bankruptcies is the formation of a committee of creditors (Chapter XI bankruptcies) and/or the appointment of a Trustee (Chapter X or straight bankruptcies) to investigate the affairs of the bankrupt and determine the best course of action for the creditors as a group.

Types of Bankruptcy

The Act of 1938, also known as the Chandler Act, encompasses three types of bankruptcy: liquidation or straight bankruptcy, reorganization, and arrangements with unsecured creditors.

The bankruptcy sections of the Law, Chapters I through VII, are designed for persons, partnerships and corporations which are deemed to be unable to continue in business. Assets, if any remain, must be liquidated and distributed to creditors in satisfaction of their claims in order for the debtor to obtain discharge from his debts.

Although the above conditions, commonly referred to as "going broke" are most commonly thought of when the term "bankruptcy" is used, there are two other sections of the law which are of equal importance. These sections, Chapters X and XI, which are referred to as the reorganization and arrangement sections of the law, are designed for businesses which are experiencing financial difficulties but are potentially profitable and sound and presumably can be continued in operation.

For the purpose of future discussion, the three types of bankruptcy discussed will be referred to as straight bankruptcy (Chapters I-VII), reorganization (Chapter X) and arrangements with creditors (Chapter XI). Chapters VIII, IX, XII, XIII and XIV deal with specialized forms of bankruptcy, such as railroad reorganizations and Maritime Commission Liens, and will not be discussed.

The distinction between bankruptcies and reorganizations or arrangements is important to the independent accountant. The former involves the audit of a company in the process of liquidation; the latter of a going concern. The distinction must be kept in mind when planning the audit field work.

The general characteristics of the three types of bankruptcy are as follows:

Straight Bankruptcy

As mentioned above, the bankruptcy sections of the Law are designed for the debtor who is deemed unable to continue in business. A corporation may voluntarily file a bankruptcy petition or may be adjudicated bankrupt upon the filing of an involuntary petition by a creditor or creditors. Involuntary petitions may be filed by one creditor, if there are less than twelve creditors, or by three creditors, if there are more than twelve creditors. Involuntary petitions may be filed only if the debtor owes $1000 or more, the petitioning creditors' claims aggregate $500 or more and an act of bankruptcy can be shown to have been committed by the debtor. The acts of bankruptcy are as follows:

1. Transfer or concealment of assets by the debtor with intent to hinder, delay or defraud his creditors.

2. Payment of antecedent debts while insolvent within four months of the filing of a petition, the effect of which is to enable one or more creditors to obtain a greater percentage repayment of his debt to the detriment of other creditors. Such payments are known as preferences.

Edward A. Weinstein, supervisor in the New York office, joined TRB&S in 1958. He is a member of the New York office practice development committee and also serves on the Insolvency and Bankruptcy Procedures Committee of the New York State Society of CPAs.

Mr. Weinstein received his B.A. from Columbia College with distinction in economics in June, 1957, and is active in the Columbia Alumni Association. He received his M.B.A. from the Wharton School of Finance and Commerce, University of Pennsylvania, in 1958.

A native New Yorker, he is married and the father of a 10 month old son.

3. Allowing liens to be obtained by any creditor on any asset of the alleged bankrupt while insolvent and failure to vacate the lien within thirty days.

4. A general assignment for the benefit of creditors.

5. Allowing the appointment of a receiver or trustee to take charge of his property when the alleged bankrupt is insolvent or unable to pay debts as they mature.

6. Admission in writing by the alleged bankrupt of his inability to pay his debts and his willingness to be adjudicated bankrupt.

The six acts of bankruptcy mentioned above are important to the independent accountant in the conduct of his examination under Chapters X and XI. During the conduct of these examinations he may find that the debtor has committed an act of bankruptcy, which act may enable the creditors to petition that the debtor be removed from Chapter X or XI proceedings and be adjudicated bankrupt.

A trustee or receiver administers the affairs of the bankrupt under Chapters I-VII.

Reorganization

Chapter X proceedings, which are only available to corporations, are reorganization proceedings. Under Chapter X the rights of all classes of creditors and of the stockholders may be affected. Reorganization differs from straight bankruptcy in that once the plan of reorganization has been accepted by two-thirds of the claim holders in each class of creditors and by a majority of the stockholders (when equity still exists), the corporation may be discharged from the proceedings and may continue in business.

Since the investing public may be affected by reorganizations under the provisions of Chapter X, the Law provides that the Securities and Exchange Commission shall become a party in interest with the right to be heard in all matters upon filing of a notice of appearance in such cases if requested or approved by the judge. In addition, the judge may submit the plan of reorganization to the SEC for examination and report thereon, if total indebtedness does not exceed $3,000,000, and must request such an examination and report if total indebtedness exceeds $3,000,000. The report on the plan by the SEC is advisory only and is not binding on the judge. However, the plan of reorganization cannot be approved by the judge until the SEC has filed its report or indicated that it will not file a report.

Petitions under Chapter X may be filed voluntarily by a corporation, or involuntarily by three or more creditors having aggregate claims of $5000 or more.

A trustee administers the affairs of the debtor under Chapter X proceedings if the corporation's aggregate indebtedness exceeds $250,000. In the cases of smaller corporations a trustee may be appointed or the debtor may continue in possession.

Arrangements with Creditors

Under Chapter XI proceedings an arrangement with unsecured creditors is sought by the debtor. An arrangement with unsecured creditors may take the form of an extension of time for payment of debts in full or a reduction of the debt, or a combination of both. In these proceedings, and under the plan, the rights of secured creditors and stockholders cannot be altered. Since the rights of stockholders are not affected in such proceedings, the SEC is not a party in interest under the law and is not required to review and report on the plan of arrangement.

As is the case under Chapter X, Chapter XI differs from straight bankruptcy in that once the plan of arrangement is approved by a majority in number and amount of unsecured claim-holders, the corporation may be discharged from the proceedings and may continue its business.

Unlike Chapters I-VII and X, petitions under Chapter XI may be filed only by the debtor. They may be filed while either reorganization or involuntary straight bankruptcy petitions are pending, either before or after adjudication.

It is usual in arrangement proceedings for the debtor to remain in possession of the company and run the business, although there are provisions for a trustee to be appointed.

Other Differences

Another distinguishing feature between the reorganization-arrangement sections and the bankruptcy sections of the Law are the provisions regarding executory contracts such as leaseholds. Under Chapters X and XI, landlords can claim accrued rent plus damages up to a maximum of the next succeeding three years' rentals; under Chapters I through VII one years' rentals. These general claims are in addition to an administration expense claim for use and occupancy during the bankruptcy.

Preference payments, (payment of antecedent debts, see acts of bankruptcy above) may be recovered by the corporation or its estate under Chapters I-VII, X or XI. These payments become important in straight bankruptcy examinations since they may represent substantial additions to the bankrupt's estate. In reorganization or arrangement proceedings they become important if they are excessive in amount, indicating possible bad faith, or can be used by the creditor's committee to prove an act of bankruptcy. Under usual circumstances, creditors in reorganization and arrangement proceedings are not as concerned with recovery of preferences as they would be in bankruptcy proceedings.

It should be noted that bankruptcy situations are very fluid. A corporation which files a Chapter XI petition and operates as a debtor in possession may be removed from this status and placed under Chapter X, or declared a bankrupt. For example, Davega Stores went from Chapter XI to Chapter X to bankruptcy; Dejay Stores went from Chapter XI to bankruptcy and Dilbert Bros. went from Chapter XI to Chapter X.

The Accountant's Role

In most cases, the independent accountant is recommended to the court by the creditors' committee or the trustee. The accountant is required to file an affidavit with the court stating the audit steps expected to be covered and an estimate of his fee. He is appointed by the court and is responsible to the court and the creditors' committee and/or the trustee. The accountant has been described as a quasi officer of the court and owes primary responsibility to it.

Since the auditor is responsible to the court, his report must include all facts which come to his attention during the examination, even if detrimental in nature to the bankrupt or debtor and/or its management. As the court appointed auditor, he is entitled to see all books and records of the company and any withholding of such books and records by an officer of the company is a fact which must be included in the auditor's report.

The accountant's report will in most cases disclaim an opinion on the financial affairs of the debtor because of various aspects of the examination which will be discussed in a later section and because of conditions encountered during the examination which cause the audit to be incomplete.

Fees

As stated previously, the accountant estimates his fee to the court in his affidavit. Once this fee is agreed to by the court, any amounts in excess of the estimate, caused by additional work not originally anticipated, must be requested from the court in an additional affidavit outlining the reasons for the additional work.

The accountant's fee is considered an administration expense and therefore receives first priority in payment along with other administration expense claims. If the estate of a bankrupt is not large enough to pay these claims in full, the accountant shares on a pari-passu basis with other administration expense claimants.

It should be noted that although an accountant's fee receives first priority under one type of bankruptcy, this priority diminishes as the debtor is removed from one type of bankruptcy and becomes subject to another. Hence, the administration expense claim of the accountant appointed under Chapter XI is secondary to all administration expense claims incurred if the company subsequently is placed under the provisions of Chapter X or declared a bankrupt, even though the accountant continues as the court examiner. A separate claim must be submitted for the work done in each phase of bankruptcy. It can be seen that the accountant would be wise to determine the condition of the debtor and the potential size of its estate as quickly as possible to protect his own interests.

Under Chapter X, as mentioned above, the SEC is considered a party in interest. As such it may object to the accountant's or other fees as being excessive in amount. This should be considered by the accountant in his determination of whether to accept such an examination and how to proceed with regard to his fee once having accepted the engagement.

The Audit

Since examinations in arrangement and reorganization proceedings are basically audits of going concerns, the ways in which these audits vary from the normal audit of a client company will be discussed first. Audit program variations in the case of straight bankruptcy will next be considered. Finally, some of the complicating factors which may arise under either type of examination will be mentioned.

Arrangement and Reorganization Proceedings

In planning his program of examination, the accountant should keep in mind the objectives of the creditors in arrangement and reorganization proceedings. In these cases the assumption is that the company will continue in business after reorganization. It is a going concern. Therefore, the creditors are interested in prior years' operations and the future potential of the business. Specifically, they will want answers to the following questions and may request the independent accountant to obtain the answers: Why did the company suffer losses in prior years? What can be done in future years to produce a profit (e.g.: cut costs, sell an unprofitable division, etc.), and what is the best possible settlement that can be expected, which will enable the company to achieve the financial reorganization necessary for its survival?

In addition, the creditors are interested in knowing the amounts of liens existing on assets of the debtor (e.g.: mortgages, factors' liens on receivables) and the amounts owed on claims which receive priority (taxes and wages). Knowledge of these facts enable the creditors to estimate the size of the initial dividend or distribution available to them.

Typically, the creditors and debtors will negotiate extensively on the settlement, which leads to another creditors' committee question: What is the approximate liquidating value of the company and therefore the lowest settlement that can reasonably be proposed by the debtor?

The accountant generally indicates the major points in his program of examination of the debtor in his affidavit. Typically, the program of examination will include all standard auditing procedures and conform to generally accepted auditing standards with these exceptions:

A) Accounts receivable usually are not confirmed. If the receivables have been factored, the accountant may request confirmation from the factor.

Typically, the accountant "reviews and analyzes" trade accounts receivable and reviews the adequacy of the reserve for bad debts. In the majority of bankruptcy examinations, which are of small and medium sized corporations, the time necessary for confirmation of receivables is not available, since the committee of creditors or the Trustee requests the accountant's report as quickly as possible in order to effect a plan of reorganization or arrangement. In the case of an examination of a large corporation, it is likely that time requirements will not be as limiting, since other aspects of the audit such as investigation of unusual transactions will be more extensive and detailed, and the accountant will be able to request confirmation of receivables. Where time is not a limiting factor, the accountant-examiner should not omit the confirmation audit step.

B) Deposits, prepaid expenses, etc. are also not usually confirmed for reasons similar to those discussed in (A) above. These accounts are usually reviewed and analyzed. Again, confirmation, if time permits, should be requested as in a normal audit.

C) No request for vendor statements is made. Since creditors are required to file their claims with the court, the accountant is often requested to compare a listing of these claims with a trial balance taken from the debtor's books and to reconcile major differences.

Although it would appear from the above that the accountant's field work is curtailed in a bankruptcy examination, this is quite contrary to most bankruptcy situations. Among the usual audit steps included in the accountant's affidavit are:

1) Review of transactions relating to investments and acquisitions and

2) Report on any significant unusual tranactions which came to the accountant's attention during the audit.

"Unusual transactions" include transfer or concealment of assets, preference payments, transactions with related parties at less than arms' length and virtually any transactions which resulted in the dissipation of the corporation's assets in a manner other than in the ordinary course of the business. Auditing these transactions and obtaining enough detail of them for the report can involve a rather large amount of effort and time.

Straight Bankruptcy

The audit of a bankrupt differs from audits in arrangement and reorganization proceedings since the bankrupt is to be liquidated. The creditors are interested in the liquidating value of the bankrupt's assets. The creditors and the court are also interested in unusual transactions which occurred prior to the bankruptcy. They are particularly interested in the question of transfer or concealment of assets by creditors or by stockholders.

The program of examination should include steps which will disclose the following:

1) Preference payments made during the four months prior to bankruptcy.

2) Sales of inventory to vendors or other creditors.

3) Sales of fixed assets.

   a) to creditors or others at less than full value
   b) to creditors as an account offset
   c) back to the manufacturer or as an account offset

4) Misappropriation of receipts, in particular, advances from factors.

5) Liens given to creditors in contemplation of bankruptcy to enable them to obtain a greater percentage distribution than other creditors.

6) Withdrawal of assets by stockholders in the form of dividends, loans, transfers of assets, etc.

7) Potential assets, such a pending lawsuits (e. g. patent infringement suits) which may increase the size of the estate, if settled favorably for the bankrupt.

8) Any other transactions which in the accountant's judgement, arose otherwise than in the ordinary course of the business (e. g., acquisitions, concealment of assets).

Conditions Encountered During the Audit

The independent accountant is likely to encounter a variety of unusual conditions which do not exist in the audit of a solvent corporation Among the conditions encountered during our recent examination of a bankrupt were the following:

1) Books and records were in a poor, incomplete condition. Transactions were not recorded completely; incorrectly recorded, and in some cases, not recorded at all.

2) Accounting personnel were completely unfamiliar with the exisitng books and records. Many of the employees had been employed for only a short period of time, turnover of employees was extensive, and morale was low since the future of the organization was in doubt.

3) There were extensive transactions with the major stockholder of the bankrupt involving cash, land, and other assets and intercompany charges. We were unable to examine the books and records of the stockholder, nor could we obtain confirmations of intercompany accounts. Our analysis of these transactions was limited to the available records, which were particularly deficient in this area.

4) There were numerous acquisitions and investments during the year prior to bankruptcy. With one exception, all resulted in severe financial strain on the company and in eventual dissipation of assets. Financing of these transactions was quite complex and neither the transaction nor the financing was always well documented or recorded on the books.

5) Although items (1) (2) (3) and (4) above are fairly common in bankruptcy proceedings, as a general rule each bankruptcy is unique in some respect. In the case of our client, our examination was further impeded by the fact that the executives who remained during the period of the court administration were unfamiliar with the financial aspects of the business and in particular with the unusual transactions which we were attempting to analyze.

Because of these conditions, it was necessary to employ some unusual audit procedures. The following methods were used in our investigation and may be useful in future audits of this nature.

1) Interviews with all people who might have knowledge of the unusual transactions being audited.

2) Inspection of all available correspondence files.

3) Inspection of all documents in the hands of the Company's former attorneys.

4) Examination of prior accountant's workpapers.

5) Confirmation of the transactions, orally or in writing by second parties.

6) Chronological scheduling of all loans (from related parties and outsiders), investments, acquisitions, intercompany transactions and other unusual transactions. This enabled us to place each of the transactions in perspective and to trace the transfers of assets into and out of the corporation.

7) Extensive tracing and retracing: comparison of different pieces of information in order to reconstruct the events which preceded and may have precipitated the bankruptcy.

The Report

The accountant's report on a bankruptcy, reorganization or arrangement examination will usually disclaim an opinion because of limitations on the scope of the examination and/or conditions encountered which cause the field work to be incomplete. The report should indicate all reasons for the accountant's disclaimer of an opinion, including a discussion of any areas of the examination which were incomplete and the reasons for not comleting the examination. Where sources other than the books and records of the corporation are used in obtaining information for the report, these sources should be documented. All transactions of an unusual nature should be described in as much detail as is possible. Finally the report should include a discussion of the reasons for the bankruptcy and in the case of arrangements and reorganizations, the possibility of continuing the business.

Conclusion

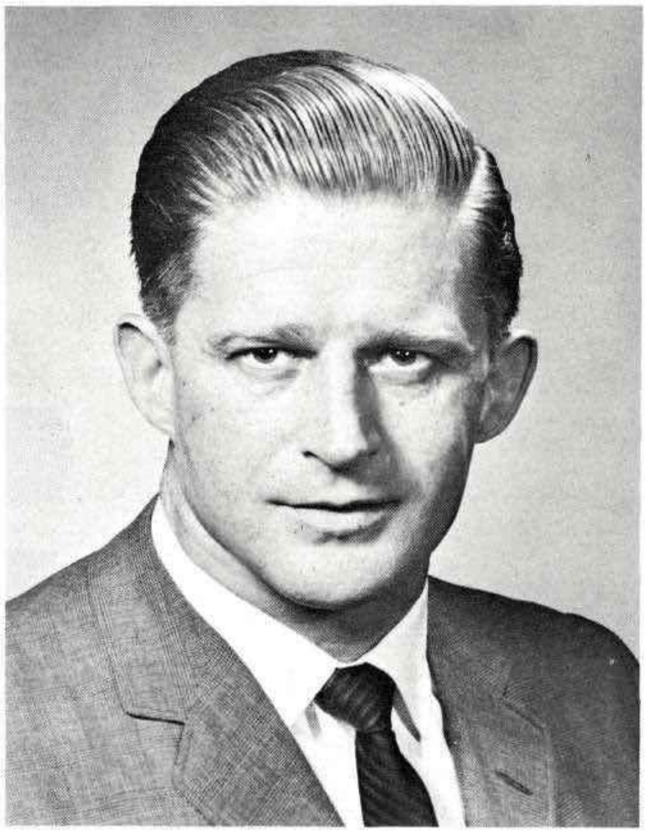
As can be seen from the above discussion, the examination of a corporation subject to any of the provisions of the bankruptcy law is considerably different from the normal audit of a client corporation. Because of the fact that his examination is conducted under the auspices of a court, and may be subject to close scrutiny in court, the accountant must take particular care in the conduct of his examination, the preparation of his workpapers and the comprehensiveness of his report.

The accountant should be thoroughly familiar with the sections of the bankruptcy law which pertain to his examination. It is almost essential that he work and consult closely with the attorney for the creditors' committee or the trustee.

This article is reprinted from The Canadian Chartered Accountant. *It is the winner of the Walter J. McDonald Memorial award, given for the best article to appear in that publication each year. The decision of the judges was unanimous.*

The Disintegration of an Information Service

Neil Milroy, C.A.



Neil Milroy is director of Management Controls with our Canadian Firm. He has been responsible for the designs and installation of a great many management control and cost systems and has also been involved in organization studies, profit improvement programs and general reviews of clients' operations. He has written articles and has given numerous lectures on integrated control systems, management accounting, direct costing and other subject of interest.

Mr. Milroy obtained his Bachelor of Commerce degree from McGill University in 1948 and his C.A. degree from the Quebec Institute in 1952. In 1957 he received a diploma in Management and Business Administration from McGill. He is a member of the Quebec Institute of Chartered Accountants, the Financial Executives Institute, and the National Association of Accountants.

ALTHOUGH ACCOUNTING is usually regarded as having a restraining influence on wasteful practices, it is sometimes disturbing to find that a limited concept of its function in corporate life is often directly responsible for one of the most insidious causes of waste in many companies: inadequate business information.

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New York and Santiago Handle Joint Engagement at Portillo....

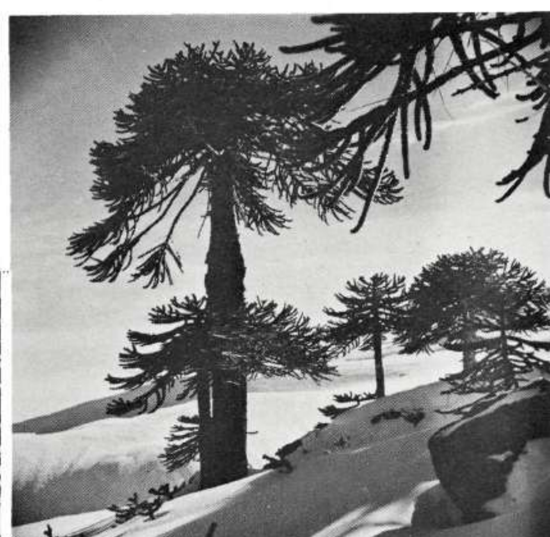
When Robert W. Purcell and Richard S. Aldrich (Chairman and Vice-President, respectively, of International Basic Economy Corporation), decided in 1960 to take over ownership and operation of Portillo, a ski resort in the Andes, they engaged our associates in Santiago, Chile to assist the local manager in all areas. Our Santiago partner, J. Francisco (Pancho) Humphreys, brought the New York office into the picture and now the two offices handle the engagement jointly.

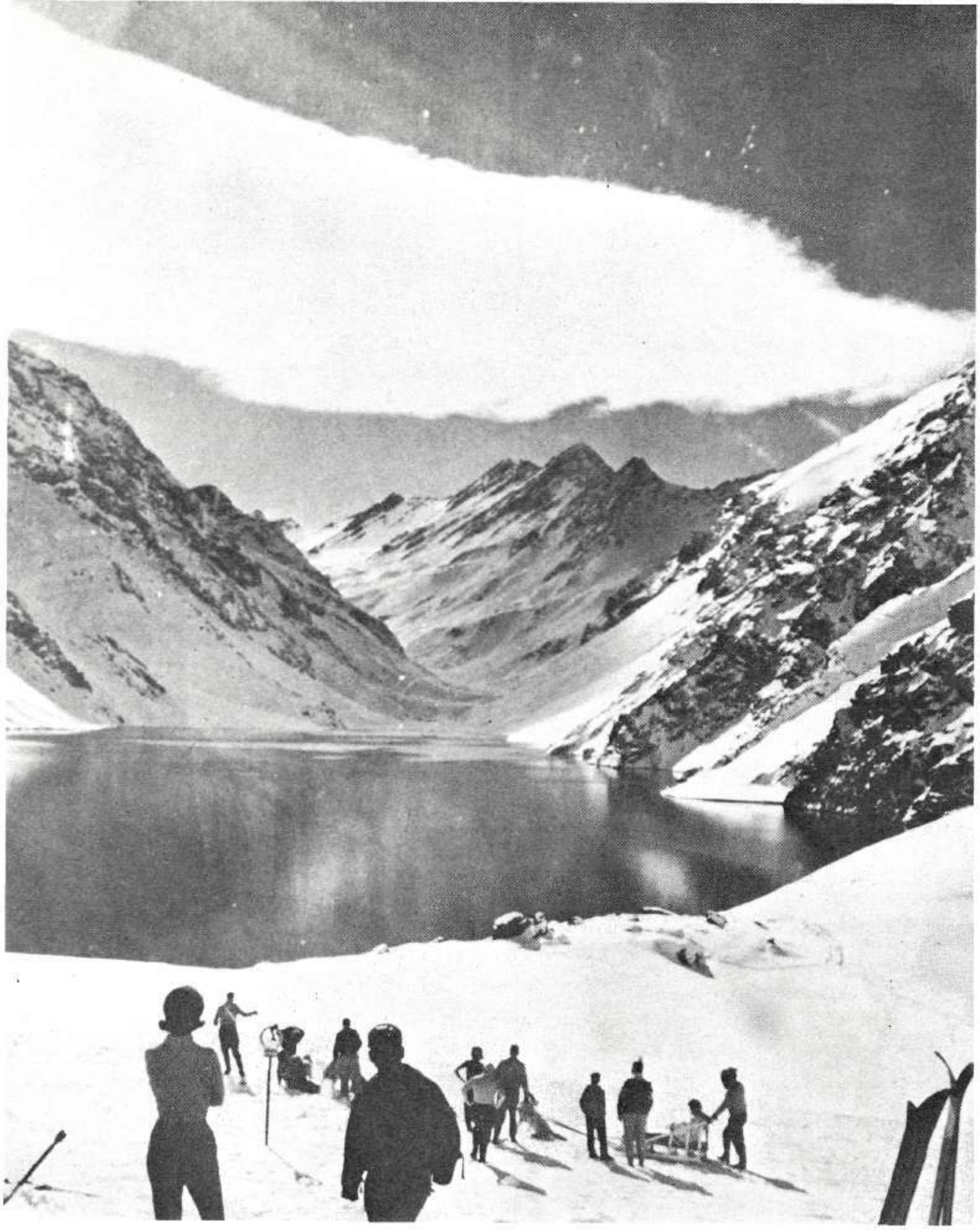
Portillo, an international ski resort with accommodations for over 300 skiers, is only five and a half hours from Santiago by car or railway. The scenery is spectacular.... Portillo is 9,400 feet above sea level and the hotel, which overlooks a lake, is protected by a circle of towering mountain crags which rise 25,000 feet or more.

Their skiing season extends from June to the middle of October, and skiers can literally ski right off the premises and on to the slopes. Portillo boasts some of the longest and steepest runs in the world, and will be the scene of the 1963 world ski championships. However, they also hold elementary ski classes on gentle slopes ideal for the raw beginner.

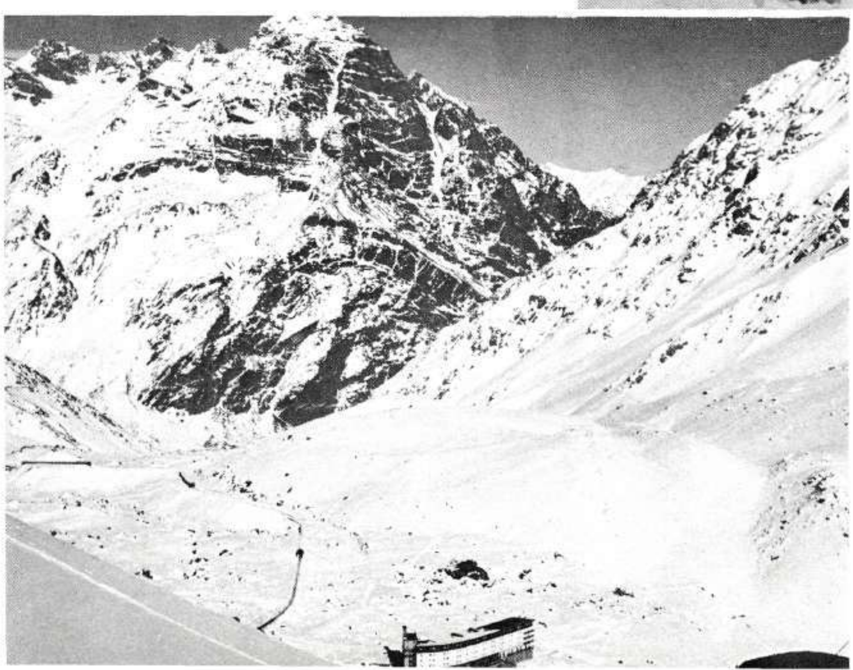
The owners are working to make Portillo an all year round resort that will appeal to both winter and summer sportsmen and vacationers. Their improvements include a skating rink, a swimming pool, a trout-stocked lake, a movie theatre, a night club and the newest in ski lifts. They have also acquired a second ski area known as LaParra, as well as a mountain side restaurant, a bus line servicing the ski resorts, and a tourist agency.

TRB&S *in Chile*





Pictured below at Portillo
are Robert W. Purcell, Mrs. Richard S. Aldr
Mrs. Purcell and Mr. Aldrich.



NEW
IN

Robert Minnear, manager in the Atlanta office, is well versed in the retail field. A graduate of Ohio State University, he joined the Dayton office of TRB&S in 1953 and transferred to Atlanta when that office was opened in 1958.

Mr. Minnear is currently serving as secretary and member of the Executive Committee of the Altanta Chapter of the Georgia Society of CPAs and is a member of the Board of Governors of the Atlanta Chapter of the Institute of Internal Auditors. He is married and has two daughters.

RETAIL ACCOUNTING is moving forward in new and diverse directions to meet today's needs. The past few years have witnessed impressive developments in computers adaptable to the needs of retailers. New second and third generation computer systems have come within the reach of many more retail organizations. Point-of-sale recorders, on-line-real-time systems and optical scanning devices all loom large on the horizon. But not all of the new developments in retail accounting are confined to electronic data processing. Late in 1962 the Controllers' Congress of the National Retail Merchants Association published the *Retail Accounting Manual.* This book contains new thinking in the areas of expense classification, management reporting, departmental operating statements and branch store accounting.

The purpose of this manual and its predecessors is the development of a uniform accounting system applicable to all retail enterprises. Since such a system must be adaptable to the management information requirements of individual stores, the need for flexibility is paramount. On the other hand, there must be sufficient discipline to insure comparison of results among the various stores using it. The system does not require of the stores uniform policies or procedures. It is not an attempt to standardize the store. The only standardization is in the measurement of the results of store operations.

CONCEPTS RETAIL ACCOUNTING

by Robert E. Minnear

History

The roots of the *Retail Accounting Manual* can be traced back to 1916 when a committee of the NRDGA began a study of expense classification. A series of committees of the Controllers' Congress has studied this topic since then and from time to time reports, books and manuals have been published—*The Classification and Distribution of Expense in Retail Stores*—1917; *A Standard Method of Accounting for Retail Stores*—1922 (revised in 1927, 1932, 1936 and 1950); in 1954 *Standard Expense Center Accounting Manual* (SECAM) and in 1962 the *Retail Accounting Manual.* Each of the manuals has added new concepts to retail accounting but has maintained an evolutionary approach. The 1954 manual introduced the now extensively used concepts of Standard Expense Centers and Production Unit Accounting.

Each manual, however, has remained true to the theme expressed in the original report in 1917:

> "The prime objective is to establish a basis of understanding between stores so that in conversing with one another, or in company statistics of operation, the terms used and the meaning attached to them may be identical to all."

Touche, Ross, Bailey & Smart has been active in this work almost from the beginning. John W. McEachren and J. P. Friedman were members of the 1927 revision committee and Mr. Friedman was a member of the 1950 revision committee. Kenneth P. Mages was a member of the 1954 Standard Expense Center Accounting Manual Committee as well as the committee which prepared the new manual.

Preparation of the new manual was a herculean task covering over three years. The value of time *donated* to writing the manual is estimated at over $400,000. But service to the many divergent businesses of the retail industry necessitated an effort of these proportions. Without the expense manuals of the NRMA, such industry-wide reports as the Harvard Report and the "Merchandising and Operating Reports of Department Stores" (MOR) would not be possible. These invaluable tools provide independent retailers with a wealth of expense and operating statistics to measure their own performance in considerable detail. The growth of the figure exchanges of AMC and similar organizations would hardly have been possible without the standardization provided by the Controllers' Congress manuals.

Multi-Store Accounting

Probably the most significant new concept in the manual is multi-store accounting. We have witnessed in the past decade the phenomenal growth of shopping center department stores which has paralleled the population flight to the suburbs. The large single unit store company which was the model for the development of standard expense center accounting is fast becoming a thing of the past. We have seen the development of so-called "chain within a chain" complexes, e.g., Burdine's seven units in Miami and Maas Brothers' eight units in the Tampa-St. Petersburg area. In past years some large dominant retail organizations seemed reluctant to start branch stores. Today most of these same companies have several units in operation. In early 1959 Rich's in Atlanta consisted of the downtown store and a diminutive twig operation sixteen miles away. Today Rich's has two large shopping center stores and will have a third in operation by the end of 1963. By 1966 Rich's five shopping center stores will circle metropolitan Atlanta.

Growth of multi-store operations demanded modification of the Standard Expense Center Accounting Manual. In fact this need prompted an entirely new manual. The principal accounting problem resulting from these organizational changes is expense distribution. Certain direct or "four-wall" expenses, such as salespersons salaries, can be identified with each selling unit of the complex and should be charged directly to the respective unit's operations. However, many other expenses, for example general management, can not be identified directly with the selling unit. Whether or not to allocate these expenses to selling units and, if so, in what manner were the points in question. In general five methods evolved:

1. Branch stores charged with direct operating expenses only.

2. Branch stores charged with direct operating expenses plus incremental expenses.

3. Branch stores charged with direct operating expenses plus overhead computed as a percentage of sales.

4. Branch stores charged with direct operating expenses plus overhead based on work load.

5. Multi-store approach to expense distribution.

Space does not permit a discussion of each method, but careful reflection will show that each is a refinement of the preceding one. Also each progressive step reflects the increasing importance of the so-called branch stores. For example, when Rich's sole branch was a small appliance store, Method 1 measured in a reasonably satisfactory manner the contribution of that outlet. Virtually no extra effort or expense was imposed on the downtown store to maintain this branch. Such is not the case with the 210,000 square-foot Lenox shopping center store. If Rich's consisted only of a downtown store and one large branch, probably Method 4 would be satisfactory; with the addition of more and more units it becomes extremely cumbersome and almost unworkable.

The multi-store approach seems to be the answer to the problem of expense distribution. Gone is the parent or downtown-branch store philosophy. Now we have a number of selling units and a central organization. The downtown store is now just a selling unit, often the biggest selling unit, but in a few years even this may change.

Under the multi-store method, all expenses which can not be charged directly to a selling unit are collected into the central organization expense pool. The expense center concept has not been abandoned but, in addition to being classified by expense centers and natural divisions, expenses must now be identified as between selling unit and central organization. Many expense centers will have two parts — one for selling unit direct expenses and the other for central organization expense. For instance, under Expense Center 110-Management, Natural Division 09-Traveling, there would be some travel costs charged directly to selling units and others to the central organization. On the other hand some expenses are mutually exclusive. Under Expense Center 110, Natural Division 01-Payroll, the president's salary could only be central expense while the selling unit managers' salaries could only be direct expenses. The chart of accounts in the manual aids in distinguishing between these two new categories of expense.

Controversy still exists as to whether the central organization expense should be distributed to the selling units. One school of thought opposes distribution of central organization expense because methods of allocation are arbitrary and the individual selling unit managers have little or no control over the central organization expense. Others think that for any operating statement of a store to be meaningful, central organization expense must first be distributed to all selling units. Only after developing a final net profit by unit can management make adequate judgments on the stores' operations and compute return on investment. The best approach seems to be a compromise. Allocation of central organization expense should be made, but probably no more often than twice a year. On a month to month or short range basis the most important figure for a selling unit is its contribution, i.e., gross margin less direct operating expenses. But annually or semi-annually a final net profit by unit should be determined.

Chart of Account Revisions

The new manual presents a streamlined chart of accounts. Expense centers and natural divisions have been retained but the old concept of more sophisticated expense center classifications for larger stores has been abandoned.

Older manuals had different charts of accounts for small, medium and large stores. SECAM had account structures for Group A, B, C and D stores, with the number of expense centers ranging from seventeen for the A Group to seventy-one for the D Group. In contrast there are only twenty-three expense centers in the new manual. This reduction in the number of expense centers does not imply that retail accounting has become simpler; rather it recognizes the impact of multi-store operations. Within the multi-store complex there are outlying selling units with streamlined and simplified organizations. It seems undesirable to change the organizational structure of these branches to conform to the more complicated expense center structure of the downtown store. This does not mean, however, that a store can not keep more detailed expense information for any given selling unit or area of expense. The accounts within any of the twenty-three expense centers can be "fanned out" and, for some portions of the larger stores, accounts undoubtedly will approach the detailed D groupings of SECAM.

There was little change in the natural divisions. A new division, fringe benefits, was added and imputed interest was deleted. Equipment rental was revised into a more meaningful division called equipment costs. Total equipment costs may now be collected into one expense center and then prorated out to the users of the services. This latter revision is a recognition of the importance of automation and electronic data processing. To the seventeen natural divisions have been added three contra credit divisions—expense transfers, outside revenues and other credits, and multi-store distribution.

The manual contains and recommends one or more alternate bases for distributing to the selling units the central organization expense charged to each expense center. This distribution of expenses is effected through the multi-store distribution account.

The increasing size and importance of fringe benefits necessitated a revision of the accountability for these expenses. An expense center previously existed for supplementary benefits for the store in total. This center still exists but the new natural division, fringe benefits, provides a means of distributing the total fringe expenses to each division so that they are not buried in expense transfers or some other category.

Another new manual concept is the use of total store sales as the basis for all percentage of sales computations. The prior practice was to express all ratios as a percentage of net *owned* department sales. The difficulty of determining the indirect expenses (real estate costs, credit, etc.) which apply to leased departments was the cogent reason for this change. Elimination of arbitrary allocations of indirect expenses to leased operations should improve comparison of statistics among stores.

Management Reporting

We may point with justifiable pride to the section on management reporting which was written by David Fleisher of the St. Louis Office. This chapter has received enthusiastic response from the retail industry. The techniques and report formats in this chapter were formulated during our survey of the management information system of Rich's. The key elements of the management reporting section are:

1. Elimination of unimportant information.
2. Comparison of actual results with meaningful management standards.
3. Good reporting formats, utilizing trend techniques.

We as accountants are all too familiar with the voluminous reports often prepared for top management. Vital information is either not reported or is obscured by a mass of detail. The busy store executive does not have the time, and should not be expected, to sort out the information he needs for decision making. For example, top management of one of our retail clients received monthly a complete set of the departmental operating statements several hundred pages in length. At our recommendation this was replaced by a two page report highlighting operating statistics by merchandise group and by department.

Too often in retailing the principal standard for comparing current results is last year's performance. The limitations of this performance standard are obvious. The model management reports use planned figures as the measure of performance against actual. Prior year's or month's figures are eliminated from the reports.

A well conceived budgetary and profit planning system is vital to the development of meaningful and useful management reports. The Core concept in developing sound profit plans is flexible budgeting. Under this budgeting philosophy expense behavior is studied and related to different levels of activity. Frequently expense budgets are geared directly to planned sales volume. Although the sales forecast is the first step in preparing the profit plan, the key to constructing flexible budgets is the determination of the most appropriate yardstick for measuring activity for each area being budgeted. Expense behavior is analyzed to determine which costs vary with activity (variable) and which do not (fixed or standby). From this intensive analysis the flexible budget is prepared for each expense center.

The activity unit selected for each expense center will probably be the same as that described in the production unit accounting chapter of the manual. Production unit accounting is not one of the new features of the manual. This technique, which is basically productivity measurement, has been used by some retailers for many years.

Two of the most important considerations in selecting measuring units for production unit accounting and flexible budgeting are:

1. The unit selected must measure the basic activity of the expense center.
2. The production measuring unit must be simple, cohesive, readily understandable, and easy to count, so that collection of data for productivity measurement will not impose an undue burden.[1]

Some examples of measuring units are gross sales transactions for Sales Audit, invoices handled for Accounts Payable, and pieces marked and remarked for Checking and Marking. Typically, retail stores collect considerable data on productivity; therefore, it follows that preparation of flexible budgets should be easier than in many manufacturing operations.

In addition to the two fundamental principles that a measurable unit of activity must be determined and a sound analysis of expense behavior be made, approval of the budget must be obtained from the individual responsible for the expenses budgeted. The latter is basic to any budgeting philosophy but is implicit in the collection of budgeted expenses by responsibility. Standard expense center accounting should provide for the necessary classification of expenses by responsibility.

A sample set of retail management reports was recently developed by David Fleisher for use in one of the Tobe lectures at the Harvard Business School and at the Controllers' Congress Convention in Philadelphia. Since it is not possible to include the model reports with this article, their titles are listed below to provide an idea of the nature and scope of these reports.

Top Management:
- Highlights of Operations
- Total Company Income and Expense Statement
- Total Company Balance Sheet
- Summary of Year to Date Store Operating Results
- Summary of Year to Date Department Operating Results

Store Operations (used only by multi-store companies):
- Income and Expense Statement by Store

Merchandising:
- Group Merchandising Summary
- Divisional Merchandising Summary
- Departmental Merchandising Summary
- Departmental Operating Statement

Operating Expenses:
- Total Company Expense Spending Variance Summary
- Expense Spending Variance Summary by Expense Center
- Expense Center Report

A complete set of these model reports is available in each office in the Retail Services Subject File (File 176.0); a review of them will provide more detailed information about the management reporting system than is contained in the *Retail Accounting Manual.*

Return on Investment

One of the principal functions of the accounting system is to provide information on the profitability of the organization. Management is vitally interested in the profitability of individual segments of the business departments and selling units, as well as the total business. The traditional yardstick is profit expressed as a percentage of sales. Equally important is return on investment which is the measure of efficiency of capital employed. In comparing the efficiency of capital utilization among businesses, complications are introduced because of varying proportions of debt, equity and rented capital. To compensate for this retailers have used for many years a device known as imputed interest. An interest charge, usually 6%, was made against operations based upon capital employed (accounts receivable, inventory and property and equipment). Imputed interest was used to put all stores on a presumably comparable basis. The contra credit to imputed interest was classified as other income, against which the debt equity charge, interest expense, was netted. Of course imputed interest was eliminated in preparing external reports, except for retail figure exchanges.

Many retailers questioned the usefulness of imputed interest and in 1962 the Board of Directors of the Controllers' Congress voted to eliminate its use. Since imputed interest has been dropped from retail accounting little purpose would be served here by a discussion of its

[1] More sophisticated techniques are advocated by our work measurement specialists. In many cases productivity should be measured by use of a group of weighted units rather than one unit. A full discussion of work measurement is available in our management services libraries.

shortcomings. Return on investment should provide much more meaningful information on the efficiency of capital utilization.

Since the early part of the last decade much has been written on return on investment. The major problem areas have been defined; techniques have been refined; and substantial agreement has been reached on many controversial areas. However, there is a need to direct research and discussion to specific needs and problems of the retail industry. Agreement must be reached on specifics such as: (1) the basis of measurement—total assets employed or equity, (2) asset valuation adjustments to be made — should lifo inventories be adjusted to fifo, how should asset reserves be handled, how should property and equipment be valued and (3) frequency of computing return on investment.

Once return on investment is computed, it is necessary to evaluate it. Goals and acceptable standards for the industry, businesses and segments of businesses must be established. Because of the free flow of information which prevail in the industry and the reasonable degree of standardization of accounting techniques, valid comparisons of stores should be attainable. It is encouraging to note that at least one major buying group has begun to compile and exchange return on investment statistics. A recent issue of "The Women's Wear Daily" headlined "Rates of Return Stressed as Key Retail Guidepost".

Absolute profit dollars and the rate of earnings on sales are not sufficient information for management to evaluate either the total business or any of its major components. The other part of the return on investment equation, capital turnover (sales divided by capital employed), must receive equal consideration. The management reports presented in the manual provide a section for reporting measures of return. This is but one phase in the overall scheme to provide management with necessary decision-making data.

Other Sections of the Manual

Other chapters of the manual not discussed here are Elements of Reports and Statistics, Departmental Statements, Determination of Gross Margin, Accounting for Workrooms, Production Unit Accounting and Special Explanations. Generally these chapters were brought forward with minor editing from SECAM. The chapter on Special Explanations should be of particular interest to our staff members who are just developing their interests and capabilities in retail accounting. This chapter includes definitions and concise explanations of the method of handling such transactions as repossessions, transfers, leased departments and allocation of central organization expense.

A special chapter has been prepared on the gross margin problems of multi-store companies. Because of the high cost and difficulty of maintaining separate inventory records by store, combined or common stock ledgers are generally used by multi-store organizations. Since separate inventory records are not kept for each department in each store, it is not possible to determine gross margin by department within each store. Under these conditions we have what is called "pooled" gross margin. A single gross margin is derived for each selling department as though the department existed in a single location. It follows then that the overall gross margin percentage for each store differs only because of the varying proportions of departmental sales in each store. Although the use of pooled gross margin and the common stock ledger has made it difficult, if not impossible, to isolate inventory shortages by store and does not produce certain data that was available from separate stocks, most large multi-unit stores believe that the effort and expense of accurately accounting for inventory transactions among the selling units is not justified.

Summary

The close association and identification of our firm with the retail industry and its importance to us should impel us to read and discuss the new manual. Staff members assigned to retail engagements must have a working knowledge of the significant concepts of the manual, particularly the newer ones of multi-store accounting, return on investment and improved management reports. To render proper service to our retail clients we must be prepared to assist them in installing these features in their information system. In some cases we will have to provide the stimulus to interest management in these improvements.

The *Retail Accounting Manual* is not an isolated text on the subject of retail accounting. As we have seen it is the latest product of an evolution which began early in this century. This is certainly not the final word on retail accounting and reporting. Members of our firm have made substantial contributions to this manual and its predecessors. We must have wide understanding and full discussion of the new concepts in retail accounting if we are to continue to contribute to its progress.

Timber and

The tax-wise owner of timber can realize capital gain from sales, exchanges or utilization of his timber. This is permitted under sections 631 and 1231 of the 1954 Code (and its predecessor provisions under the 1939 Code). This article will discuss some of the tax planning problems which may be encountered in obtaining the advantages of section 631. Space limitations do not permit as full a discussion as may be desirable, but a list of additional references is appended.

Need for Legislation

Before discussing the present rules of section 631, some historical perspective should be helpful. Prior to 1944, a mill operator could obtain a capital gain benefit only by an outright sale of timber which was a capital asset or an asset used in his trade or business. Also an investor could obtain a capital gain benefit only by an outright sale of timber. Neither could obtain a capital gain benefit if he was a dealer. Since private sales of timber usually involve a considerable amount of money, an outright sale was difficult to conclude.

To overcome this problem timber was sold on a pay-as-you-cut basis. That is, a cutting contract was executed granting timber cutting rights for a unit price per thousand board feet (MBF). This procedure raised the question of whether the consideration was for the sale of timber or a royalty. The Treasury related timber (a natural resource) to mineral deposits and held, as in the case of mineral leases, that the payment represented a royalty and as such was ordinary income despite the fact that the timber was a capital asset in the hands of the taxpayer.

This situation depressed the wood products industry because investors wanted to make only outright sales of timber and small operators could not meet the terms. Mill operators with their own stands of timber were reluctant to cut and create ordinary income out of the appreciation accruing during a long holding period. To a certain extent this resulted in mill operators selling blocks of timber back and forth to attain a tax saving even though such sales would result in an economic loss because of the location of the exchanged timber.

Congress concluded that the law discriminated against taxpayers who disposed of timber by cutting it as opposed to those who sold it outright. In order to eliminate this discrimination, the Senate added to the Revenue Act of 1943 an election which permitted the taxpayer who for more than 6 months before the beginning of the year had owned timber or had a contract to cut timber to treat

Stanley Gullixson

Taxation

the cutting of timber as a sale or exchange. A disposal of timber, held more than 6 months, with a retained economic interest would be treated as a sale of property used in the taxpayer's trade or business. Timber which qualified under these amendments would be considered property used in a taxpayer's trade or business. The effect of these amendments was to provide capital gain treatment for the sale of timber whether outright or on a cutting basis.

In 1944 Congress reached agreement on this proposal for the taxation of timber and what would be section 117(k) of the 1939 Code went to the President. In vetoing the bill, President Roosevelt stated: "As a grower and seller of timber, I think that timber should be treated as a crop and, therefore, as income when it is sold. This would encourage reforestation." In successfully urging overriding of the veto, Senator Barkley stated, after noting that the President sold Christmas trees: ". . . to compare those little pine bushes with a sturdy oak, gum, poplar or spruce, which requires a generation of care and nurturing to produce in the forest, and from which no annual income is derived until finally it is sold, is like comparing a cricket to a stallion."

Stan Gullixson, manager in our Portland office, is a specialist in the tax problems of timber operators and owners. He graduated with highest honors from the University of Oregon in 1951, receiving a B.S. degree.

An active member of the Timber Valuation Liason Group, he also serves on the following committees of the Oregon Society of Certified Public Accountants: Taxation; Legislation Policy; and Tax Forum. He is married and has two daughters.

Section 117(k) was re-enacted in the 1954 Code as Section 631. One of the changes made in the section was to define timber as including "evergreen trees which are more than 6 years old at the time severed from the roots and are sold for ornamental purposes."

Cutting of Timber

Section 631 covers two situations — the cuttting of timber and the disposal of timber with a retained economic interest.[1] Section 631(a) allows the mill operator to elect

[1] Section 631 has no effect on the applicability of the regular capital gain and loss provisions. Thus, sales or exchanges of an interest in timber, not qualifying under section 631(b), but held as an investment which qualifies as a capital asset, will result in a capital gain or loss, long or short term, depending on the holding period.

on his return to treat the cutting of his timber as a sale or exchange. The timber which is so treated is considered property used in the taxpayer's trade or business. Under section 1231 the net gain on sales and exchanges of property used in a trade or business is taxed as a capital gain and a net loss is deductible as an ordinary loss. Therefore, if timber gains or losses and other section 1231 gains or losses result in a gain, the gain is a capital gain. If they result in a loss, the loss is an ordinary deduction. The cyclical nature of the wood products industry makes the tie-in with section 1231 extremely important because of the limitation on capital loss deductions.

Timber cut during the tax year must be held 6 months prior to the beginning of the year in order to qualify under section 631(a). If the election is made, all the timber cut during the taxable year is presumed to have been sold as of the first day of the year. In order to determine the section 631(a) gain, it is necessary to determine fair market value as of the first day of the taxable year and to compare this with the adjusted basis for depletion of the timber cut during the year.

The fair market value of timber cut during the year becomes the cost of the timber for all purposes. Thus, it is necessary to redetermine inventory cost for tax purposes, but this should not exceed market if the cost or market method was elected. When the end product which was the subject of a section 631(a) election is sold, the gain or loss realized is ordinary income or loss.

Inventory cost adjustments are usually made on a MBF basis. Lumber and plywood footages are converted back to log footages based on operating conversion results and the ending inventory is presumed to contain a pro rata portion of section 631(a) timber and timber not qualifying under the section. This determination may be made on a company wide basis or on a plant basis so long as the method is consistent.

Information for the Tax Return

In the preparation of a tax return involving section 631(a), two additional schedules are generally provided. The first presents the excess of the fair market value of the timber cut over the cost depletion and supports the gain reported on Schedule D. The second presents the required adjustments to the beginning and ending inventories and supports the Schedule M adjustment. The section 631 changes to be made to a conventional tax return can best be understood by journal entry presentation as follows:

(1) Depletion		$200,000	
Capital gain (Sec. 1231)			$200,000
To record additional depletion and gain under section 631(a) as follows:			
Fair market value of timber as of January 1, 1962	$500,000		
Cost depletion of timber cut	300,000		
Additional depletion	$200,000		
(2) Cost of sales (beginning inventory)		12,000	
Surplus			12,000
To record prior year's section 631(a) gain in the beginning inventory.			
(3) Surplus		15,000	
Cost of sales (ending inventory)			15,000
To record current year's section 631(a) gain remaining in the ending inventory.			

Illustration of Section 631(a)

To show the importance of section 631 to a mill operator, three examples are presented below for a corporate taxpayer and an individual taxpayer assuming no other section 1231 gains or losses and that all timber cut was sold. In these examples the difference between the fair market value at the beginning of the year of timber cut during the year and the cost of such timber (section 631 (a) gain or loss) is treated as realized in a sale or exchange of property used in a trade or business. Under section 1231, the gain is treated as a capital gain and the loss is deductible as an ordinary deduction.

As can be noted from the above examples, there is a greater advantage to noncorporate taxpayers because the additional depletion lowers the tax bracket with the added advantage of a 50% capital gains deduction. This does not necessarily mean that a mill operator should not incorporate, but does point up the difference in tax rates. The saving to a corporation of 27% (52% — 25%) is well worth the effort. To illustrate this point, Treasury Officials appearing before the House Ways and Means Committe reported the 1961 tax rate of Weyerhaeuser as 27%, Georgia Pacific 28% and U.S. Plywood 30%.

	A	B	C
Corporate taxpayer			
Taxable income	$200,000	$200,000	$200,000
Depletion adjustment under 631(a)	100,000	(100,000)	400,000
Balance before 631(a) gain or loss	$100,000	$300,000	$(200,000)
Section 1231 loss (ordinary deduction)		100,000	
Subject to normal and surtax	$100,000	$200,000	$(200,000)
Subject to alternative capital gains tax	100,000	—	400,000
Taxable income	$200,000	$200,000	$200,000
Income tax without 631(a)	$ 98,500	$ 98,500	$ 98,500
Income tax with 631(a)	71,500	98,500	98,500(2)
Individual taxpayer (3)			
Subject to normal and surtax (as above)	$100,000	$200,000	$(200,000)
50% of capital gains	50,000	—	200,000
Taxable income	$150,000	$200,000	Nil
Income tax without 631(a)	$156,820	$156,820	$156,820
Income tax with 631(a)	92,320	156,820	Nil

(2) Alternative tax not used since it is more than normal and surtax.

(3) To simplify the problem, it is assumed that the taxpayer has income from other sources equal to his other deductions, including exemptions.

Needless to say, the elimination of taxable income in example C for a non-corporate taxpayer, will be examined closely by the Treasury Department.

Two important conclusions can be drawn from the examples: first, there is everything to be gained and practically nothing to be lost under section 631(a) and, second, tax planning will reap benefits.

Planning for an Election Under Section 631

The possible detriment of section 631(a) involves other section 1231 gains in that the capital gain benefit will be lost if 631(a) losses offset the other 1231 gains. Since this rarely occurs in any material amount and can be mitigated by planning, it can safely be stated that the election of section 631(a) will result in a tax saving in the long-run and should be adopted by every mill operator. Some tax advisors have attributed another detriment to 631(a), that of accelerating income. If the timber is cut and on hand at year end, thereby requiring an increase in the year end inventory valuation, income is created prematurely. This is a factor, especially in the first year under the election when there is no corresponding adjustment to the beginning inventory, but is a limiting factor only and does not overcome the advantage of the election.

The tax planning is very basic: maximize 631(a) gains and maximize 631(a) losses so as to avoid having 631(a) gains offset 631(a) losses in any taxable period. Concentrate the cut of high cost timber during poor economic years since the 631(a) loss is an ordinary deduction. Concentrate the cut of low cost timber during good economic years so that full benefit can be obtained from the resulting 631(a) capital gain but endeavor to avoid a situation where the alternative tax on the 631(a) gain exceeds the ordinary tax on the taxable income. The planning of a loss through cutting high cost timber must take into consideration the adjustment provisions pertaining to operating loss carrybacks and carryovers in order to assure full benefit from the loss.

It should be noted that, under the regulations, timber is not considered cut when it is actually cut. It is considered cut when the quantity of timber felled is first definitely determined in the ordinary course of business.

Acquisitions of timber should not be grouped into one block and one depletion rate, since this destroys all possibility for a mill operator to plan for minimal income taxes. The quantity of timber in a tract is normally determined by a professional cruiser at the time the timber is purchased. The depletion rate is determined by dividing the MBF into the purchase cost less an apportionment to land. The depletion rate can be by specie (spruce, fir, hemlock) or an over-all rate. The selection of the method depends upon the quantity of minor specie in the tract and the contemplated method of logging the tract. Generally, a separate rate for each specie facilitates production planning as well as planning section 631(a) gains.

Method of Election

The election to use the provisions of section 631(a) is made in the return for the taxable year to which the election is to apply. The form of the election is simply to make the computations to comply with the provisions of the section. The election applies to all timber the taxpayer owns or has a contract right to cut, which is held more than six months prior to the beginning of the taxable year in which the timber is cut. The cut timber (logs) must be used in the taxpayer's trade or business which can include the sale of the logs. The election is binding to subsequent years unless permission is obtained to make the change.

The fair market value of the timber cut during the year is determined on the first day of the taxable year, and is defined as the sale price between a willing seller and a willing buyer, assuming a sale on the particular day. This determination is subject to all the problems of establishing fair market value for other assets and, in addition, is subject to a determination of the cost incurred in converting the timber to logs and transportation to market. The best method of establishing timber fair market values is to use reported government sales in areas where these sales are made. Government agencies are required to appraise timber to be sold. This appraisal takes the form of determining the value of the end product and all costs incurred, going back to the standing tree. The actual government sale, together with the appraisal costs, can be used by the taxpayer, for comparison, in determining the fair market value of his own timber.

Disposal of Timber

The dealer, investor and operator can benefit from the provisions of Section 631(b) which governs sales of timber where the seller retains an economic interest in the timber. The timber is considered to be property used in the trade or business, whether the taxpayer has a trade or business or not, and is, therefore, subject to the provisions of section 1231.

If an economic interest is not retained then the transaction does not come under section 631(b) and the protection to a dealer is lost. The timber may otherwise qualify as a section 1231 asset or as a capital asset depending upon the circumstances.

The taxpayer selling timber must forego the receipt of a fixed total sum for a block of timber and accept instead a sale of the timber on a unit basis in order to qualify under section 631(b). The consideration under the contract must be determined on a unit basis, i.e., the amount of timber cut, rather than a total basis. An economic interest is evidenced by the fact that the taxpayer looks to a severance of the timber for a return of his investment.

Holding Period

There is no election to come under 631(b); if you meet the requirements of the subsection, its application is automatic. In order to qualify, the timber must be held for more than six months prior to disposal. (Not six months before the beginning of the taxable year, as under subsection (a)). The 1954 Code added a definition of disposal. Regardless of the contract date, the disposal date is deemed to be the date the timber is cut. It is, therefore, possible for a taxpayer to purchase standing timber one day and sell it under a contract with a retained economic interest the same day, and all timber cut under the contract more than six months after the purchase date can qualify for capital gains treatment under section 1231. (As in the case of subsection (a) the date timber is cut means the date when in the ordinary course of business the quantity of timber felled is first definitely determined).

Advances and Minimum Payments

Cutting contracts granting to the purchaser the right to cut all or a particular specie in a specified stand of timber and requiring payment on the basis of a fixed amount per unit generally will qualify. This does not mean that the seller cannot receive advance or periodic minimum payments under the contract, but these payments must be applied against units of timber actually cut under the contract.

Providing the conditions of section 631(b) are otherwise met, advance and minimum payments are treated as realized from the sale of timber, if the timber for which the payments apply is cut more than six months after the date of acquisition. If the buyer can not perform under the contract and forfeits some portion of the advance or minimum payments, the amount not applied to actual units cut is ordinary income to the seller. Amended returns must be filed when necessary.

Election for Alternate Disposal Date

When payment is received before the timber is cut the owner may elect to treat the payment date as the disposal date. The election is made by attaching a statement to a timely filed return (including extensions) for the period in which the payment is received identifying the payment and the contract.

If the payment date would provide more than a six month holding period there would be no purpose for the election since the cutting date would also provide more than six months and nothing would be changed by the election. However, if the payment date would not provide more than a six month holding period then the election would take that payment out from under the provisions of section 631(b).

When the payment represents a gain, the gain could be used to offset other types of losses that would otherwise expire. If a loss, the loss could be used to offset or reduce other types of income. It should not be presumed that the election will convert the gains and losses into ordinary gains or losses since the disposal dates and provisions of section 631(b) do not apply. Careful consideration should be given to the terms of the contract, provisions of local law and the business of the seller.

Basis of Timber

As in subsection (a), the taxpayer determines basis or depletion rate on a per unit basis. In the case of advances or minimum payments, basis is allowed in accordance with the number of units paid for by the prepayments. If a bonus is paid under the contract, the basis for the bonus proceeds is determined by applying a fraction to the total basis of the timber to be cut; the numerator of which is the amount of the bonus and the denominator is the total expected proceeds under the contract including the bonus. If part of the timber is cut prior to the required six months holding period, the bonus must be pro-rated to this period based on footage.

As the disposal date is now deemed to be the cutting date, it would appear to be possible to see timber not in existence at the contract date and satisfy the requirements of section 631(b). However, the Internal Revenue Service has recently ruled that the proceeds would be ordinary income and a final determination must await litigation. It would be necessary to satisfy local laws as to what constitutes a sale and still avoid a royalty classification.

Time for Reporting

Neither the payment date election of disposal nor other provisions of section 631(b) have any effect on the time for reporting gain or loss.

Gain or loss is reported when payment is received or accrued unless the terms of the contract and the provisions of local law clearly make the consideration other than royalty or lease payments.

The Future of Section 631

In June 1963, while considering the President's 1963 tax message, the House Ways and Means Committee killed the administration's plea for a sharp cutback in the capital gains allowance on timber. In reporting the Committee's action, Representative Al Ullman (D-Ore.) said: "Treasury admitted its position was not sound after the Forest Service said its proposal would seriously affect reforestation."

READING REFERENCES

Section 631 and regulation 1.631 — Gain or loss in the case of timber or coal.

Section 611 and regulation 1.611-3 — Allowance for deduction for depletion.

Regulation 1.611-3(f) — Determination of fair market value of timber property.

Section 1221 and regulation 1.1221 — Capital asset defined.

Section 1231 and regulation 1.1231 — Property used in the trade or business and involuntary conversions.

NYU 18 — Institute on Federal Taxation (p.577) Tax Aspects of Timber Transactions by Thomas V. Lefevre.

L. D. Wilson (26 TC 474) — Retained economic interest.

Ah Pah Redwood Co. — (251 F. 2d 163) — Holding period and capital assets status.

Revenue Ruling 56-434 — Fair market value of timber and application of section 631 to tops and limbs.

Revenue Ruling 57-90 — Application of section 631(b) regardless of taxpayer's business of purpose or which the timber is held.

Revenue Rulings 62-81 and 62-82 — Sale and lease distinguished, timber not in existence and retained economic interest.

President's 1963 Tax Message (House Ways and Means Committee Print) Page 382 — Tax treatment of timber.

Faces in the News

Donald Wiese (left) of our Boston office was one of five CPAs who appeared on a color television program to answer tax questions phoned in by viewers. The program called "Your Federal Income Tax", was part of the "Dateline Boston" series over WHDH-TV, Channel 5 in Boston. The panelists were all members of the Massachusetts Society of CPAs.

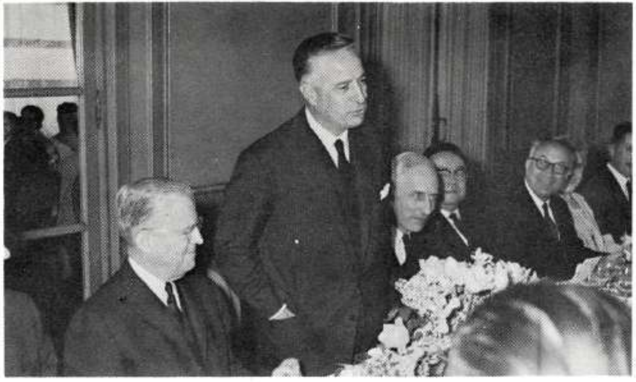
In July the Detroit office conducted a seminar for the Japanese Finance Management Study team now on a world tour in connection with the Tokyo Management Association. Shown above are Professor Shigeo Aoki, Waseda University; Gwain H. Gillespie, partner in the Detroit office; Kinzo Hirota, president of the tour group; Donald W. Jennings, partner in the Detroit office. Henry E. Bodman (not shown) also spoke.

Walter H. Soderdahl (left) partner in the Chicago office, shakes hands with George H. Kern, resident partner, Lybrand, Ross Brothers & Montgomery, as Harlow E. Bowes partner of Sidley, Austin, Burgess & Smith, looks on. Mr. Soderdahl acted as discussion leader at a workshop session on "Filings with the Securities and Exchange Commission" sponsored jointly by the American Institute of CPAs and The Illinois Society of CPAs. It was geared especially for the small practitioner with special emphasis given to first filings.

CHICAGO DAILY NEWS

William Schwanbeck, shown with wife, Florence, served as general chairman of the Sixtieth Annual Meeting of The Illinois Society of Certified Public Accountants held at the Drake Hotel in Chicago June 9-13. Mr. Schwanbeck was responsible for all technical sessions of the meeting and for the entertainment. Approximately four hundred people were in attendance.

Dennis G. Price from our New York office joined two other EDP specialists and traveled to Nashville, Tenneesee to examine that state's data processing system for finance. Shown here are (left to right) Harlan Matthews, Commissioner of Finance and Administration; William P. Snodgrass, State Comptroller; Governor Frank G. Clement; Dennis G. Price; J. L. Dorman, Director, EDP, New York State; Robert Hooper, IBM, Albany, N. Y.



Our associated firm in France held their 30th Anniversary celebration recently. John W. McEachren, (left) Chairman of our Policy Group, attended the festivities in Paris. E. G. Snozzi, head of the Paris office, is shown speaking.

Charles T. Horngren, professor of accountancy at the University of Chicago, was one of the speakers at the TRB&S Management Conference held in Hot Springs, Va., July 16 to 26. Professor Horngren, noted for his published articles and papers, was faculty resident in our Chicago office.

PHOTO FROM MEXICAN NEWSPAPER NOVEDADES.

Pictured here are (left to right) Ramon Perez Alonso, Emmett H. Heitler, Executive Vice President of Shwayder Brothers, Inc., Juan Perez Alonso, Arthur Samelson, partner in charge of the Denver office, and Domingo Alonso.

The Alonso's are officers of a Mexican corporation that is negotiating a contract with Shwayder Brothers for the manufacture of Samsonite luggage in Mexico.

Luella (Peg) Wood, first Detroit office employee to retire under the firm's retirement plan, was honored at a party at the Detroit Golf Club on August 1. Miss Wood joined George D. Bailey and Company as switchboard operator and receptionist when the firm was organized in 1947. She continued in that capacity as the office grew and became well known to people in the firm. She is shown here with Donald W. Jennings, partner; Harry G. Troxell and Paul E. Hamman, partner in charge. Miss Wood's retirement plans include a trip to Switzerland in the near future.

The TRB&S EDP Study Task Force held training sessions recently in San Francisco, Chicago, New York and Dallas. IBM's Elliott Greene conducted technical sessions on functions of computers. Programs covered computer concepts and functions as well as the problems and techniques of auditing EDP-maintained accounting systems. The computer demonstration was photographed in Dallas.

Sixty-two Staff People Promoted

MANAGERS

Donald R. Best, Milwaukee
Miles H. Bresee, Jr., Phoenix
Millard L. Breiden, Philadelphia
David V. Burchfield, Detroit
William J. Byrne, Philadelphia
John P. Carroll, New York
Joseph T. Casey, New York
David L. Fleisher, St. Louis
W. Donald Georgen, Chicago
William E. Griscom, San Francisco
William J. Grismer, San Francisco
Norman C. Grosman, Los Angeles
Nicholas Kunycky, New York
James M. Lynch, Boston
Ira A. H. Osman, Jr., Phoenix
Herbert M. Paul, New York
Raymond E. Perry, Chicago
Andrews C. Ries, St. Louis
Lowell L. Robertson, Milwaukee
Harvey E. Schatz, Detroit
William R. Sutherland, Milwaukee
Misag Tabibian, New York
Donald L. Trawicki, Milwaukee
Richard F. VanDresser, Detroit
Donald E. Visconti, Philadelphia
Donald C. Wiese, Boston
Charles E. Wieser, Detroit

SUPERVISORS AND SENIOR CONSULTANTS

James F. Ascher, Minneapolis
Ronald J. Bach, Minneapolis
John J. Balian, Los Angeles
Kenneth L. Brown, Kansas City
Robert C. Estes, San Francisco
Robert M. Furman, New York
Paul J. Gerry, Boston
Robert P. Gibbons, New York
John W. Hauch, Chicago
George J. Heberer, Milwaukee
Gerald B. Jackson, Kansas City
William R. James, Detroit
Donald M. Keller, Boston
William H. King, San Francisco
Carl M. Koster, Los Angeles
Robert C. Lane, Los Angeles
Thomas I. Marcosson, New York
Maurice L. McGill, Kansas City
James V. Mitchell, Seattle
Robert K. Mitchell, Phoenix
William E. Neeley, Portland
Gerald W. Padwe, New York
Jean-Paul Ruff, Executive Office
Robert J. Sack, Dayton
Edward Sallerson, Rochester
Carl E. Sturgeon, Chicago
Norman E. Swenson, Seattle
Charles G. Taylor, Jr., Dayton
John VanCamp, Chicago
David J. VanderBroek, Detroit
Alexander Varga, Executive Office
John L. Vernon, Executive Office
Edward A. Weinstein, New York
Grant M. Woodfield, Seattle

With Alumni . . .

Boston — Richard A. Farrar, a former member of the audit staff, has assumed the position of controller with a Boston client the Vermont Tap and Die Co. (a division of Bermont American Corporation), in Lyndonville, Vermont.)

Peter J. Power resigned to accept a position as assistant to the general manager of Ebsco Industries, Inc., in Red Bank, New Jersey.

Walter T. Barker resigned from the audit staff in July to take a position as assistant controller at the Wesson Memorial Hospital in Springfield, Mass.

Chicago — Ronald Stone resigned from our audit staff to accept a position with our client, The Greyhound Corporation.

Dayton — Donald Boomershine has been appointed controller of the Texarkana Division of Divco-Wayne Industries.

James Sauer and Douglas Strain have resigned their positions on the Dayton office audit staff to accept assignments with a client of the firm, The Rike-Kumler Company. James is in charge of the internal audit function, replacing Gene Roberts, a former employee who has been promoted to assistant to the executive vice-president. Douglas is the assistant office manager.

David Dern resigned to become controller of Six Industries, Springfield, Ohio.

Zane Haught resigned to join a local accounting firm, R. S. Thompson & Company, in Richmond, Indiana.

Conrad Weinrich, an alumnus of the audit staff, has been promoted to manager of the systems and procedures department of The Mead Corporation.

Denver — Andrew Jakes left the Denver office to go back to Denver University to participate in a Masters Program. After completion of the course he will take up a teaching career.

Detroit — Four staff members have left the firm recently for responsible positions with clients:

Donald O. Nellis moved to Portland, Oregon, to become assistant controller of Evans Products Company. On July 1, James H. Dunbar assumed the position of controller of Flint Ink Corporation in Detroit. Edwin H. Hicks has joined American Motors Corporation as assistant manager of the tax department. In May, John P. Tierney was named chief accountant of Pioneer Finance Company.

Executive — Joseph Levee resigned to accept a position with Socony Mobil Oil Co., as senior research and planning analyst in the tax department.

Grand Rapids — William N. Dahlquist, who had been with the Grand Rapids office for five years, resigned to take a position in Chicago with Bell & Howell Co., as manager of the internal audit department.

Milwaukee — Kenneth W. Rammer left the firm to accept a position as controller for a client, Aluminum Specialty Company, in Manitowoc.

Minneapolis — Lee Christoffersen left to take a position as business manager of the United Christian Churches of America office in Minneapolis.

On September 1, Donald Etnier will take up his duties as Assistant Professor in accounting at the Arkansas State College at Jonesboro, Arkansas.

New York — Seymour Flug resigned to assume the position of assistant controller at Kerkeby-Natus Corporation.

Pittsburgh — Gary B. Fink, a senior on the audit staff, left the firm to become asssistant to the controller at McCreary Tire & Rubber Company, a Pittsburgh office client.

San Francisco — George English left our firm to accept a position as controller for the Russell Markets in Hayward, California.

John Kadlecek, formerly of our San Francisco and Denver offices, dropped in to say "hello" recently. He is now associated with McMurtry Mfg. Company in Denver as controller. They are a client of the Denver office.

Washington — Hugh Cochrane has accepted a position with Stewart's Incorporated, a client. Tom Fox has resigned to join a local accounting firm.

Jack Rihtarchik, audit manager in the Washington office and one of its first staff members, resigned August 1 to accept a position as Controller with Documentation, Inc.

Applause . . .

Atlanta — Robert E. Minnear is the new chairman of the Bulletin Committee of the Georgia Society of CPAs for the year 1963-64.

Boston — Donald M. Keller spoke recently before the junior class of the Amos Tuck School of Business Administration, Dartmouth College. His subject was "Carrying on a Management Services Practice."

The Massachusetts Society of CPAs has appointed Charles H. Noble to serve on its Committee on Education, and James M. Lynch to serve on the Committee on Cooperation with Bankers.

Chicago — The following members of the Chicago Office staff have been appointed to the indicated committees of The Illinois Society of Certified Public Accountants for the 1963-64 year:

Robert S. Kay, 1964 Annual Meeting; Raymond E. Perry, Auditing Procedures and Accounting Principles; Donald Hausman, Federal Taxation; Stephen I. Finney, Long Range Planning; Glen R. Ostdiek, Management Services; Gilmour M. Krogstad, Meetings Planning; Royal L. Cox, Membership; Richard H. Gallagher, Personnel; Allen C. Howard, Professional Conduct; Raymond J. Revers, Professional Development; William J. Schwanbeck, (Vice Chairman of Committee), Society Insurance Plans; Raymond P. Bloom, State Auditing and Accounting Principles; Glenn J. Hartung, State Taxation.

In addition, Kay H. Cowen has been nominated for election as a director.

Joanne Loftus has been appointed to the Board of Directors of the Chicago Chapter of the American Society of Women Accountants for 1963-64.

Robert Trueblood addressed the 1963 Annual Meeting of the Indiana Association of Certified Public Accountants at French Lick Springs, Indiana. The subject of his talk was "The Future of the Accounting Profession" and summarized in part the activities of the Long-Range Objectives Committee of the American Institute.

On June 6th, Justin Davidson addressed the luncheon meeting of the American Statistical Association's Chicago Chapter on "The Use of Modern Statistical Techniques in Accounting Practice." On the 7th, he participated in a panel discussion of the "Consulting Profession" at the annual alumni meeting of the Graduate School of Industrial Administration of Carnegie Institute of Technology.

Robert Trueblood has been appointed chairman of the accountants division for the Crusade of Mercy Campaign to be conducted this fall in the greater Chicago area.

Allen Howard has been named a member of the Accountants' Committee for the American Cancer Society Bequest Program.

At the Sixtieth Annual Meeting of The Illinois Society of CPAs, Raymond Bloom took part in a panel discussion covering the year's developments and the profession's current problems in accounting principles, auditing procedures and the latest trend in S.E.C. accounting policies. Robert Trueblood participated in a panel of A.I.C.P.A. council members discussing the present national interests of the A.I.C.PLA. Council and the impact in Illinois. As a member of the entertainment committee, Stephen Finney was in charge of "Club 60".

Dayton — Leon J. Sachleben was chairman of a panel on "Taxes of Today and Tomorrow" at the August 5th meeting of the Dayton Chapter of The Ohio Society of CPAs. Francis J. Schubert was a member of the panel.

The following from the Dayton office staff were appointed chairmen of committees of the Dayton Chapter of The Ohio Society of CPA's: L. W. Buenzow — Bylaws Committee; D. W. Charles — Committee on Cooperation with P.A.S.O.; Keith A. Cunningham — Education Committee; Herman J. Olt — Long Range Planning Committee; C. G. Taylor, Jr. — Public Relations Committee; and Irl C. Wallace — Management Service Committee. As chairmen of these committees, they are automatically on the same committees of the State society.

Irl C. Wallace participated in a panel discussion on accounting for non profit organizations, sponsored by the Community Chest of Dayton. Sixty-eight of the local agencies were represented. Mr. Wallace's topic was "Budgeting and Forecasting."

Denver — Carleton H. Griffin addressed a luncheon meeting of the Colorado Society of C.P.A.'s on May 13. His talk was entitled "Travel and Entertainment Expenses — Latest Regulations."

U.S. Marine CH-46A Sea Knight Helicopter Makes First Landing on U.S.S. GUADALCANAL

A United States Marine Corps CH-46A Sea Knight helicopter, designed and produced by the Boeing Company's Vertol Division, (client of our Seattle office) became the first aircraft to land on the flight deck of the U.S. Navy's new amphibious assault carrier U.S.S. Guadalcanal (LPH7) at Philadelphia's U.S. Navel Base.

The twin turbine transport helicopter was brought aboard the U.S.S. Guadalcanal to be on static display during the commissioning ceremonies at the Navy Base.

Designed to carry transport helicopters for Marine vertical assault missions, the U.S.S. Guadalcanal can accommodate eight of the CH-46ASea Knights on its flight deck and twenty-one Sea Knights on its hanger deck. The Guadalcanal is capaple of delivering a battalion landing team of 2,000 Marines. Each aircraft can carry 25 fully equipped combact troops.

On June 21 Mr. Griffin spoke at the annual meeting of the Wyoming Society of CPA's on "Purchase, Sale or Liquidation of a Corporate Business."

Detroit — Kenneth S. Reames was elected president of the Michigan Association of CPA's at the annual meeting at Mackinac Island in August. Mr. Reames will also serve as vice-chairman of the Committee on Nominations.

Other appointments to committees of the Michigan Association of CPAs for the year 1963-64 are: Accounting and Auditing Procedures — William S. Harter (chairman); Annual Meeting — Daniel J. Kelly; Relations with Attorneys — John D. Hegarty; Relations with Bankers — Nile W. Farnsworth; Relations with Educators — Elmer M. Houghten; Federal Taxation — David J. Vander Broek; Graduate Study Conference — Richard F. Van Dresser; Joint Review — Al M. Mlot; Advisory Committee on Legislation — Henry E. Bodman II; Management Services — David V. Burchfield; Membership — Harry G. Troxell; Personnel — Rosemary Hoban; Professional Education — Gwain H. Gillespie (vice-chairman); Professional Ethics — Paul E. Hamman; Publication — Donald H. Waterman; Public Service and Information — Phyllis E. Peters and Robert D. Wishart; State Taxation — Lyman B. Curtis; and Unauthorized Practice — Charles E. Wieser.

Nile W. Farnsworth traveled to Louisiana State University in Baton Rouge, where he spoke at the School of Banking of the South on "Special Tax Problems Confronting Banks."

Kenneth S. Reames discussed "The Proposed Substantive Regulations on Travel and Entertainment Expense Deductions" via tele-lecture before a group of students in The Nebraska Center for Continuing Education at The University of Nebraska. While Mr. Reames was speaking from his office in Detroit, pictures taken of him in his office were shown to the students.

John D. Hegarty spoke to members of the Detroit Chapter of the Tax Executives Institute at their May 22 meeting on "Travel and Entertainment Expenses." On June 20, Mr. Hegarty participated in a panel discussion at the Milk and Ice Cream Accounting Conference in Detroit sponsored by the International Association of Ice Cream Manufacturers and the Milk Industry Foundation on "Travel, Entertainment and Gifts."

Donald A. Curtis addressed the Fourth National Conference on Banking Automation in Detroit on "Lease vs. Purchase of Computer Equipment." Mr. Curtis also spoke to The Bank Women's Conference, sponsored by the Women's Committee of the Michigan Bankers' Association, in Boyne City, Michigan about "Operating Techniques in the Bank of the Future." On June 19 Mr. Curtis spoke on "The Responsibilities of the Production Control Department" before the American Production and Inventory Control Society in Detroit. Later, on June 26, he participated on a panel discussing "Operations Research and Operational Accounting" at the National Convention of the Data Processing Management Association in Detroit.

David V. Burchfield and Robert F. Worley were recently elected to the board of directors of the Detroit Chapter of the Society for the Advancement of Management for 1963-64. Mr. Worley was subsequently elected secretary of the board.

At the annual meeting of the Citizens Research Council of Michigan, George D. Bailey was re-elected a trustee and Kenneth S. Reames was re-elected a director and assistant treasurer.

Executive Office — Touche, Ross, Bailey & Smart held a seminar for several hundred top management executives of the IRI (Instituto Reconstructione Industriale) group in Rome, Italy, in June. The subject material was Advanced Business Systems. Roger Crane and Dick Sprague coordinated the work of organizing the seminar, conducted in Italian and English with simultaneous translation. Bruno Gimpel and Jean-Paul Ruff also participated. IBM, Sperry Rand, International Computers and Tabulators of U. K., Olivetti, Westinghouse and Barclays Bank participated in lectures on equipment and case studies of Advanced Business Systems.

Joseph Buchan gave a talk on scientific inventory management at a meeting of the North Eastern Section of the National Society for Cooperatives in Harrisburg, Pennsylvania.

Roger Crane was wind-up speaker at the controller's conference of the National Association of Food Chains which was held in Montreal.

Grand Rapids — Recent appointments to committees of the Michigan Association of CPAs included Richard W. Lamkin to the Committee on Professional Education, Robert P. Fairman to the Committee on State Taxation, and Joyce E. Cowman to the Committee on Membership.

Joyce E. Cowman was recently elected secretary of the American Woman's Society of Certified Public Accountants and president of the Grand Rapids Chapter of the American Society of Women Accountants.

Houston — C. A. Blankenburg has been appointed editor of the Houston Chapter News for the National Association of Accountants, and is currently serving as a director of the Houston Chapter of the N.A.A. Ray de Reyna is his very able assistant. Mr. Blankenburg was recently made a director of the Greater Houston Convention and Visitors Council, a non-profit organization designed to promote Houston as a convention city. Mr. Blankenburg has also been appointed chairman of the Finance and Budget Committee for the 1964 Convention of the Financial Analysts Federation to be held in Houston next April.

Owen Lipscomb is serving as vice chairman of the professional division of the United Fund of Harris County for the current year. He has accepted appointments to the 1963-64 Texas Society Committee on Federal Taxation, Subcommittee on Professional Practice; the Ethics Committee of the Houston Chapter of the Texas Society of CPAs; and the Program Committee of the Business and Estate Planning Council.

Mr. Lipscomb spoke before the Estate Planning Council of Beaumont on May 2. His subject was "Prudent Tax Planning During Estate Administration."

Herbert J. Brewer was appointed to the 1963-64 Committee on Membership of the Texas Society of CPAs.

Thomas C. Latter is serving on the Federal Taxation Committee of the Houston Chapter, Texas Society of Certified Public Accountants for the year 1963-64. He is also vice chairman for the 1963 Tax Institute and chairman of the Houston Section of the 1963 Institute, sponsored by the Texas Society of CPAs.

Leland C. Pickens has accepted appointment as a member of the National Organization and Regional Boundaries Committee of the Budget Executives Institute for 1963-64.

Ramon J. de Reyna is currently serving on the Management Services Committee of the Houston Chapter of Texas Society of CPAs.

Kansas City — John D. Crouch was elected president of the Missouri Society of CPAs at the 54th Annual Meeting of the Society held in St. Louis June 17 and 18.

Mary J. McCann was elected associate editor of *The Woman CPA*, official bi-monthly publication of the American Woman's Society of CPA's and American Society of Women Accountants.

Los Angeles — Richard C. Stratford was elected president of the Roscomare Valley Association, a community property owner's organization.

Vern Hakola spoke to Hawaiian bankers on June 24 on "Current Trends in Banking."

Frank Daft was elected a director of the California State Society of CPAs for a two-year term.

Memphis — Clinton R. Pearson, Roy L. Gates, Don F. Stark and Kenneth J. Gordon have been selected by the board of directors to the Tennessee Society of CPAs to serve as consultants on the CPA Consultation Service, a recent innovation of this society.

Milwaukee — Walter F. Renz was elected president of the Milwaukee Chapter of the National Society for Business Budgeting for the 1963-64 year. In addition, he has been elected president of the Milwaukee Chapter of the National Association of Accountants.

On May 14 Donald Trawicki addressed the Sangamon Valley Chapter of the National Association of Accountants at Decatur, Illinois on "Profitability Accounting."

Chester Brisley held a seminar for the Syracuse, New York Chapter of the Society for the Advancement of Management. His subject was "Work Measurement and Profitability Accounting."

During the week of June 17 to 21 Donald Best, Robert Nienow and Donald Trawicki conducted sessions of a Profitability Accounting Seminar sponsored by the Management Institute at the University of Wisconsin in Madison. Donald Jennings of the Detroit office was the conference leader.

Chester Brisley contributed to this seminar on June 20 with a talk on "Work Measurement." On June 21 in Milwaukee Mr. Brisley spoke before the executive committee of a group of presidents of small businesses ($15 million and under); his subject was "Work Measurement and Profitability Accounting."

Minneapolis — Robert Mooney served as an instructor for a Professional Development Course on Estate Planning presented by the Minnesota Society of CPAs.

Clayton Ostlund will serve as chairman of a seminar on Ethical Problems at the Minnesota Society of CPA's Annual Meeting. Palmer Tang is also participating in this seminar.

Kenneth Schuba has been elected secretary of the Minneapolis Chapter of Budgeting Executives Institute.

Delwyn Olson was named outstanding director of the Minneapolis Junior Chamber of Commerce for the year and has been appointed vice president for the coming year.

Robert Mooney spoke on "Depreciation Guide Lines and Investment Credit" at the spring meeting of the Minnesota Society of Industrial Engineers. He is also participating in a seminar on Problems of Post Mortem Estate Administration.

New York — Arthur Michaels spoke to the Accounting Club at the College of the City of New York. His topic was "Your Career in Public Accounting."

The following members of the New York Management Services Staff spoke at a three day institute in Mechanization of Welfare Functions, sponsored by the New York State Department of Social Welfare: Dennis E. Mulvihill, Dennis G. Price, John Carroll and Robert Arnold.

Herbert Paul spoke at the Sixth Biennial Conference on Charitable Foundations sponsored by New York University. His topic was "What to Do When The Revenue Agent Appears to Make An Audit." Mr. Paul has been selected to serve on the State Taxation Committee of the New York State Society of CPAs.

Victor Brown spoke at an executive seminar of the National Association of Small Business Investment Companies on August 26th at the University of Wisconsin. The topic of his talk was "Analysis and Interpretations of Financial Statements of Small Business Companies." When he spoke before a group of bankers at a financial seminar for bank executives sponsored by the Irving Trust Company, his subject was "Establishing Profit Goals." Mr. Brown spoke on a similar subject at a seminar for industrial financial executives at another seminar sponsored by the Irving Trust Company. He spoke on "Management Reporting for Retailers" at a meeting of the New York Metropolitan Controller's Association. On May 2 he spoke at the 30th Annual Conference of the Credit Management Division of NRMA held in Dallas. The topic of his talk, "What the Credit Manager Should Know About Financing Receivables."

Robert Beyer and Victor Brown co-chaired a week long Profitability Accounting seminar held by the AMA at the Hotel Astor in New York. Robert Gibbons and Robert Burton of the New York Management Services staff and Joe Buchan of Executive office also spoke at the seminar.

Robert Burton spoke before the National Convention of the Controller's Congress of NRMA at Philadelphia. His topic was "The Use of Mathematics in Retail Inventory Management."

William Werntz was a featured speaker at the SEC Regulation Institute at the University of Denver College of Law. His discussion covered selected topics in SEC aspects.

Dennis Price recently addressed a group of foreign visitors at the Sixth Administrative Management Institute held in Albany, New York. The Institute was sponsored by the Graduate School of International Affairs, University of Pittsburgh, and the address was concerned with the steps involved in making a computer feasibility study and installation.

Bernard Cianca has been nominated to fill the unexpired term of former U. S. Senator John Milton on the Jersey Public Market Commission. Mr. Cianca has also been elected a member of the accounting committee of the Greater New York Fund, and a member of the retail accounting committee of the New York State Society of CPA's.

The talk Gregory Boni gave before the Financial Management Roundtable in Washington, D. C. on March 26 will be published in a forthcoming issue of The Internal Auditor. The subject is "How Practical Are Scientific Techniques?"

COMMITTEE APPOINTMENTS OF THE NEW YORK STATE SOCIETY OF CPAs ARE:

Carson, W. K.; Cianca, B. J.; Heft, E.; Michaels, A.; Werntz, W. W.; Gerver, E.; Brown, V. H.; Blank, F. L.; Carroll, J.; Casher, H.; Cohen, P. H.; Ehling, J.; Furman, R. M.; Fertsch, C.; Frye, C. R.; Goldenberg, S.; Isola, R. A.; Marcosson, T. I.; Radin, A.; Paul, H. M.; Weinstein, E. A.; Members in Industry and Commerce; Retail Accounting; Relations with Security Dealers; Professional Conduct; Cooperation with the Bar; Federal Taxation; Cooperation with Educational Institutions; Accounting Machinery; Credit Granters; Labor Union Accounting; Hotel, Club & Restaurant Accounting; Arbitration & Mediation; Municipal & Local Taxation; Interim Audits; Stock Brokerage Accounting; State Tax Other Than New York; Fiduciary Accounting; Cost Accounting & Inventory Methods; Staff Accountants; N. Y. State Taxation; Insolvency & Bankruptcy.

Philadelphia — Lawrence J. Scully is chairman of a panel on tax accounting problems for the University of Pennsylvania Tax Conference to be held September 24, 25 and 26 at the Barclay Hotel in Philadelphia.

Phoenix — George Post represented the Arizona Society of C.P.A.'s at a recent meeting of the Western Region of the Internal Revenue Service in Los Angeles.

Miles H. Bresee, and Ira Osman were panel leaders at a seminar held at Grand Canyon College, Phoenix. Their subject was "Special Tax Problems of Small Business Men." Mr. Osman was also a panel member on a recent television program pertaining to opportunities for young people in the business world.

Howard Neff has been elected treasurer of the Arizona Retail Controllers Association. The Arizona Association has been adjudged the outstanding group in its field by the National Controllers' Congress.

Robert K. Mitchell and Howard Neff have been appointed as board members of the Phoenix Chapter, National Association of Accountants, responsible for special activities.

Pittsburgh — Louis A. Werbaneth addressed the Kingsport Rotary Club in Kingsport, Tennessee on the subject of "Expense Accounts — a Two-Part Story." He also gave the keynote address before a three-day meeting of the corporate financial staff and plant accountants of American Saint Gobain Corporation in Kingsport.

William J. Simpson, in conjunction with the Pittsburgh Chapter of the Pennsylvania Institute of CPAs, spoke to the accounting students of St. Francis College. His topic was "Problems of a Tax Practice." He has been elected a member of the board of directors of the Pittsburgh Chapter of the National Association of Accountants.

John C. Williams spoke before students of Aliquippa High School on "Accounting as a Profession." He is teaching Accounting for Specific Purposes to students at the Graduate School of Business Administration, University of Pittsburgh, on a part-time basis.

Jack C. Thomas addressed the Student Accounting Association of Duquesne University on April 24. Mr. Thomas discussed his first six months' experience in the employ of a CPA firm.

Portland — On June 21 Bill Neely gave a talk before NOMA on "Topics of Interest in Financial Management." Mr. Neely also spoke before the Eugene Chapter of the N.A.A. on "Accounting for Management Information."

Lee Schmidt was elected treasurer of the Portland Retail Controllers Group for 1963-64. Also, (for the third consecutive year), he has been elected to the Budget Study Subcommittee for The United Good Neighbors. The function of this committee is to review the budget requests and recommend allocations to the various member organizations of the UGN.

Davison Castles was appointed chairman of the auditing committee of the Portland Chapter of NOMA for the coming year.

Rochester — The Rochester area chapter of the New York State Society of CPAs has elected Gail N. Brown to the office of vice-president for the year 1963-64.

At a technical discussion held by the Society with loan officers of area banks, the opening presentation was given by James M. Moore.

St. Louis — Edwin H. Wagner was appointed a member of the Legislative Committee of the St. Louis Chapter of the Missouri Society of CPAs. Lynn Phegley was appointed a member of the Professional Ethics Committee, and Kenneth Bauer was elected second vice-president.

Mr. Bauer was also appointed a member of the Council.

Eugene Schorb served as a sergeant at arms during the Rotary International Convention held in St. Louis on June 9 to 14. 60 countries were represented at meetings held at the Kiel Auditorium. G. Basu of our Calcutta, India office was appointed vice-chairman of the balloting committee.

Dave Fleisher spoke at the NRMA Controllers Congress Convention in Philadelphia — subject — Management Reporting for Department Stores. Mr. Fleisher is with the Management Services Department in the St. Louis office.

John F. Bruen was elected first vice-president of the Missouri Society of CPA's at the annual convention.

San Diego — Raymond D. Taramasco has been appointed to the Management Services Advisory Committee and Raymond D. Johnston has been appointed to the chairmanship of the Auditing Committee of the San Diego Chapter of the California Society of CPAs.

San Francisco — Richard Nishkian acted as a discussion leader at an AICPA Professional Development meeting on filings with the SEC. The meeting was held at the Hilton Inn on July 8 and 9.

Thomas B. Wall has been appointed chairman this year for the 1963 Graduate Study Conference held at the University of California at Santa Barbara, August 21-23.

Paul Kadden addressed the San Francisco Tax Club on "Problems in Computing the Foreign Tax Credit."

Joseph S. Burns has been in Frankfurt, Germany for two months to teach quantitative techniques in a management training program for the German personnel of Trans World Airlines.

The following have been appointed to serve as members of committee for the California Society of Certified Public Accountants: Milton Gilmore — Accounting & Auditing Procedures; Leroy Schadlich — Chairman of the Committee on Taxation; and Thomas Wall — Graduate Study — Chairman Coordinating Committee — Savings & Loan. Mr. Wall has also been appointed to serve as Chairman on Professional Ethics — for the San Francisco Chapter of Certified Public Accountants.

Gene Englund is on the Educational Standards and Student Relations Committee of both the California Society of CPA's and the San Francisco Chapter. Richard Nishkian is on the Committee for Cooperation with Credit Grantors of the San Francisco Chapter. William Grismer is secretary of the Taxation Committee. Paul Kadden is also on the Taxation Committee.

San Jose — T. J. Ennis spoke before the Rotary Club of Salinas, California on June 11 on the subject "Is it a Sin to Make a Profit?" Incidentally, he left with his audience the definite impression that it isn't, and that as CPA's, we're aligned with businessmen to help them improve their profit making potential. On June 17, he spoke before the Arizona Society of CPAs on the subject of "A Consulting Service for CPA's." Mr. Ennis is a member of the Committee on Consulting Service of the AICPA.

Felix Probandt served as a member of a panel of experts, including members of the bar and representatives of the Internal Revenue Service, which discussed, before the San Jose Chapter of the California Savings and Loan League, the problems savings and loan associations can expect as a result of the new Internal Revenue Code and Treasury Department regulations. Mr. Probandt was also featured speaker at the regular meeting of the Santa Clara County Estate Planning Council in May.

Seattle — Gerald Gorans will head the professional division of the United Good Neighbor campaign. This division will probably be responsible for raising $200,000.

Durwood Alkire was a featured writer in the June issue of C/M, diary of the Concrete Masonry Industry. His article was entitled "The Investment Credit Against Federal Incomes Taxes." He also spoke on the investment credit at a meeting of the Plywood Controllers and Treasurers in Portland, Oregon. In Seattle he spoke on the same subject at the Milk and Ice Cream Accounting Conference sponsored by the International Association of Ice Cream Manufacturers, the Milk Industry Foundation, and the dairy industry associations of the states of Washington and Oregon. Mr. Alkire is also the new chairman of the taxation and revenue committee of the Municipal League of Seattle & King County for the coming year. He was appointed on July 11 to a citizens committee to review the budgeting practices of the Seattle School Board.

The Washington Society of CPA's committee appointments for the coming year include several members of the Seattle office: Durwood Alkire — Legislative; Robert Benjamin — Accounting Principles; Gerald Gorans — Chairman, Auditing Standards; Guy Pinkerton — Relations with Bar; Edward Rich — Acquaintance, Visitation & Arrangements; Norman Swenson — Federal Taxation; Dean Thornton — Chairman, Legislative and Grant Woodfield — Speakers Bureau.

Washington — Karney Brasfield participated in a panel discussion and addressed the School of Management at the 1963 convention of the International Council of Shopping Centers, held in Montreal, Canada.

TRB&S People Pass CPA Examinations

Chicago

James Burk
Robert Caudill
Norbert Florek
Jack Himel
William McMillan
John Mulhern
Donald Teigen

Dayton

James C. Bresnahan
Therll W. Clagg
J. Lawrence Fleck

Detroit

Harvey E. Schatz
David M. Smith
Frank H. Tranzow

Houston

James F. Harp
Bert McElreath
George A. Weber

Kansas City

Ronald E. Boyce

Milwaukee

Stephen Findley
Ralph A. Mirsberger
Robert Hollman
Thomas McGraw
Terry C. Balderson
Robert C. Stenman

Seattle

Dean L. Kampe
Gary A. McLean
Patrick J. Peyton
John M. Sangster
J. Garth Wheeler

Quarterly Correspondents

Atlanta, *Martha Martin* • Boston, *Marjorie J. Johnson* • Chicago, *Sherle Swanson* • Cleveland, *Alberta Everett* • Dallas, *Sallie Poole* • Dayton, *Leslie Earley* • Denver, *Beverley Thomas* • Detroit, *Harry G. Troxell* • Executive office, *Florence Tramutola* • Grand Rapids, *Joyce E. Cowman* • Houston, *Jeanie Lannom* • Kansas City, *Genevieve Silady* • Los Angeles, *Jay Liechty* • Memphis, *Ann Agee* • Milwaukee, *Mayme Solberg* • Minneapolis, *Alice Carlson* • New York, *Joan Norton* • Philadelphia, *Betty Gillard* • Phoenix, *Ira Osman* • Pittsburgh, *Mary Jo Reinbold* • Portland, *Grace McLean* • Rochester, *Marion Snyder* • St. Louis, *Lillian Meyer* • San Diego, *Wilhelmine C. Livingston* • San Francisco, *Vilma Jenson* • San Jose, *Pat Skelton* • Seattle, *Helen B. Lilly* • Washington & Baltimore, *Jean Colp*